

# Home truths

The case for rebalancing toward better means testing

Amy Auster, Henry Williams, Indra Parta and Nicholas Tarrant

June 2026



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## Acknowledgements

This report was written by Amy Auster, Henry Williams, Indra Parta and Nicholas Tarrant. We are grateful for significant contributions from Tim Murray and Phil Harslett of Precision Economics, who supported the development of the microsimulation model that underpins much of the analysis in this report, and from Manya Mediratta and Chloe Wong. We thank the senior public servants, academics and stakeholders who generously gave their time to review and challenge our work.

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This report may be cited as: Auster, A., Williams, H., Parta, I. & Tarrant, N. (2026), *Home truths: The case for rebalancing toward better means testing*. Policy Institute Australia.

ISBN: 978-1-923649-02-6

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# 1 Executive Summary

Australia's social safety net has long reflected a simple idea: taxpayer-funded support from government should go to those who need it most. That idea, grounded in our national values of fairness and equity, is quietly losing ground.

Over the past decade, social transfers have grown by over \$6,000 per Australian household in real terms. A substantial share of this has flowed to Australia's most well off households. Taking one example, a retired couple with a \$5 million home in Sydney can qualify for the full Age Pension worth almost \$50,000 a year, and up to \$150,000 for one spouse in Aged Care. Their neighbours who rent a modest home and hold \$1.5 million in super receive no pension at all and roughly half the Aged Care support.

This is not an isolated anomaly. It is the predictable result of means testing rules that have not kept pace with a wealthier and older Australia – and a quiet but significant shift in how government support is delivered.

Australia stands out among our OECD peers for achieving reasonable income equality, a relatively low tax burden, and a strong social safety net. This reflects policy choices long grounded in a social and political commitment to fairness. Our cash transfer programs, where the 20% of least well off Australian households receive 40% of cash benefits, embody this approach.

Australian taxpayers also fund a comprehensive system of non-cash supports (or 'in-kind transfers') – health and education, as well as disability, aged care and child care services. Successive governments have expanded these programs over the years, but relative to cash transfers – JobSeeker, Family Benefits – they are poorly targeted.

Whether considering the above wealthy retired couple with access to full Aged Care benefits or a family with two kids earning \$400,000 a year qualifying for up to \$20,583 in Child Care Subsidy support and about \$20,000 in Parental Leave Pay, the largesse provided to the most well-off Australians stretches the system's sustainability, as well as our social compact.

In-kind transfers are growing fast. Over the ten years to 2026–27, in-kind transfers are set to rise by 62% in real terms to reach \$305 billion, increasing from 8.3% to 10.4% of GDP. Over the same period, cash transfers are expected to grow by 10% in real terms to \$165 billion, declining from 6.6% to 5.6% of GDP.

This growth of in-kind transfers is in part due to means testing rules that are no longer fit for purpose. They are inconsistent, unevenly applied and ignore housing as a primary generator of wealth. Our choices are leaving taxpayers with a rising bill to fund services for relatively well-off Australians, and to disproportionately support Australians who own their home relative to others.

This is a concern for the fairness of our social safety net today, and for its sustainability in the years to come.

This paper proposes alternative approaches to means testing for income and wealth, applied to four programs: the Age Pension, Aged Care, the Child Care Subsidy, and Parental Leave Pay. These were chosen because they are large, are currently means tested but with poor targeting, and offer sufficient data to estimate the impact of alternative means tests.

This analysis is not intended to provide a definitive answer on means testing design for these programs. The aim is to illustrate the magnitude of the loss in equity and sustainability from our current approach, and to suggest changes that could be applied to these programs as well as others.

For each program, we have developed and modelled several means testing options. Application of an asset means test is relevant for Aged Care and the Age Pension, where wealth is significant. It is less relevant for Parental Leave Pay or the Child Care Subsidy when recipients tend to have lower wealth even when incomes are relatively high.

Our alternative means tests build on existing frameworks rather than replacing them, making the changes practical to implement.

Under current settings, the Child Care Subsidy and Parental Leave Pay are means tested by income but with very high thresholds. Less than 1% of households have incomes high enough to disqualify them from both the Child Care Subsidy and Parental Leave Pay. Australian taxpayers will pay about \$2.6 billion this year to households with incomes of \$300,000 per year or more in Child Care Subsidy and Parental Leave Payments.

For Aged Care and the Age Pension, current means testing incorporates assets held, but with great variability. Contrary to popular perception, the owner-occupied home is taken into account, but with highly preferential treatment.

A retiree with a \$3 million home is entitled to the same pension as another retiree with a \$300,000 home. A retiree who owns a \$1.5 million home with no other assets would receive the full pension, while another retiree who rents but holds \$1.5 million in shares and super would get no pension. Our approach evolves the treatment of owner-occupied housing, along with a new policy to ensure all retirees can maintain their standard of living through retirement.

## Findings

Our proposed alternative means tests would result in reduced outlays for these four programs of about \$21 billion in the 2025–26 financial year, or 17% of current funding. The majority of this reduction comes from the top 20% of households by wealth or income. We argue that these households have the capacity to contribute more for the services they are receiving, and should do so.

The scale of potential savings is significant. Freeing up \$21 billion in this financial year from these four programs could:

- Provide close to \$5,000 each year in benefits to each of the 4.4 million households in the bottom 40% of households by income or wealth.
- Fund meaningful increases in supports for those most in need — in 2025–26, total expenditure on JobSeeker was \$16 billion and on Rent Assistance it was \$7 billion.
- Cut the tax rate for all income tax thresholds by 1.7 percentage points, which would reduce personal income taxes by up to \$2,000 for Australians in the middle income bracket and up to \$8,000 for those in the top bracket.
- Pay down about 70% of the Commonwealth's fiscal deficit this financial year.

Better targeting through means testing also improves the equity in the distribution of these benefits. We assess this by comparing the benefits provided to the least well off 20% of households as against the most well off 20% of households, by income or wealth. Well-targeted cash transfer programs are already highly equitable; for example, the least well off households on Disability Support Pension and Carer Payments receive 3.5 times more benefit in these

programs than well off households. The ratio for JobSeeker is 4 times.<sup>1</sup> By contrast, in the four programs we considered, the least well-off households receive at most 1.9 times the benefit that is received by the most well-off. Our proposed approach results in a distribution of benefits that is more in line with well-targeted cash transfer programs.

To the extent that program savings are redistributed through tax cuts, the most well off households could experience little change. In our modelled example, a family with household income of \$247,000 (the median of the top 20%) could lose \$5,600 in child care subsidy benefits but gain up to \$4,300 in tax savings.

### Policy innovation: Retirement Contribution Scheme

With regards to the Age Pension, our proposed approach would result in about 2% of retiree households having an increase in their pension. About 17% would experience a reduction, or 500,000 households.

For households in the top 20% of the wealth distribution with wealth above \$1.8 million, the *average* reduction would be about \$26,000 a year. For households in the 60–80% quintile, the average reduction would be about \$7,500 a year.

We recognise that some retired households primarily hold their wealth in their owner-occupied home, and may be unable to fund living expenses at the full pension rate of \$31,200 per year for singles and \$47,100 per year for couples.

To address this, we have proposed a new policy: the ‘Retirement Contribution Scheme’, or, ‘ReCS’. Like the Higher Education Contribution Scheme (HECS) that allows eligible students to defer university tuition fees, ReCS would enable retirees to defer the cost of self-funding their retirement.

<sup>1</sup> Australian Bureau of Statistics (2018).

Like HECS, ReCS would be an opt-in scheme for retirees to access an interest-free loan against any assets – shares, super, investment properties or their home. The loan is income-contingent, with repayment deferred until there is capacity to do so through an asset sale – with no forced sales. The scheme would be government-run, easy to opt-in, and open to any Australian above the age of 67 with sufficient assets against which to secure the loan. It would fund up to 150% of the full pension rate for singles or couples, minus any pension they receive.

ReCS would ensure that retirees can maintain their living standards, but at a lower cost to taxpayers as the expenditure is eventually repaid.

### Fairer means testing

The rest of this report is organised as follows.

**Section 2** documents how Australia’s social safety net has drifted away from equity, with rapidly growing in-kind transfers that are poorly targeted and disproportionately benefit the most well-off Australian households.

**Section 3** examines current income and assets means tests across major transfer programs, including the special treatment of owner-occupied housing.

**Section 4** presents our proposed reform options for the Child Care Subsidy, Parental Leave Pay, the Age Pension and Aged Care, along with their estimated distributional and fiscal effects.

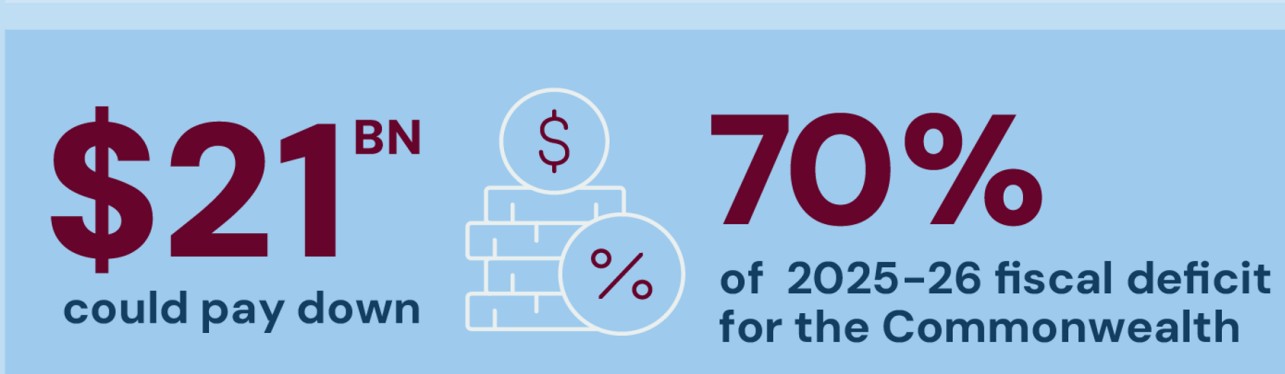
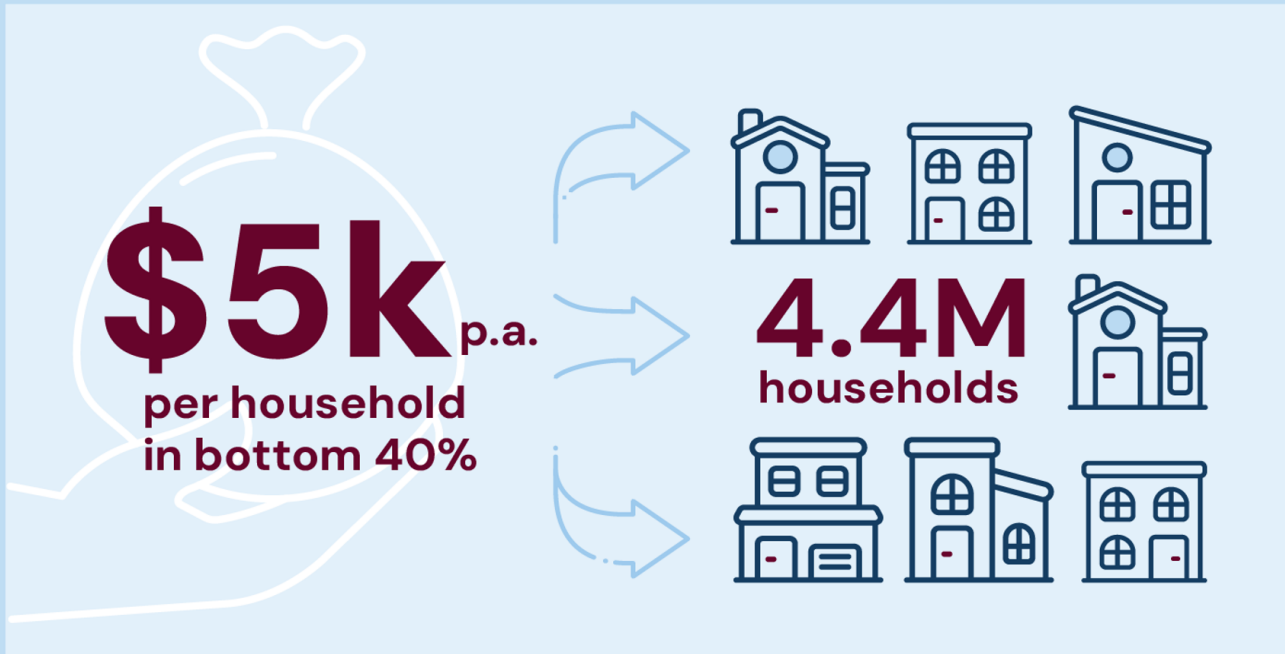
**Section 5** introduces the Retirement Contribution Scheme, ReCS, that would enable retired Australians to defer the cost of self-funding their retirement, improving the equity and sustainability of the Age Pension and Aged Care.

**Section 6** concludes the report.

## KEY POINTS

- › This paper models alternative means tests for four major programs that currently have poorly targeted means testing – the Child Care Subsidy, Parental Leave Pay, the Age Pension, and Aged Care, informed by the dual principles of equity and sustainability.
- › Better targeting of these four programs could save about \$21 billion in 2025–26, with most savings coming from the top 20% of households by income or wealth. We argue that these households have greater capacity to self-fund the services they receive.
- › The potential savings of \$21 billion could:
  - › Provide close to \$5,000 in additional support for each of the 4.4 million households in the bottom 40% of households.
  - › Fund meaningful increases in JobSeeker (which currently costs \$16 billion) or Rent Assistance (which currently costs \$7 billion);
  - › Cut the tax rate for all income tax thresholds by 1.7 percentage points, which would reduce personal income taxes by up to \$2,000 for Australians in the middle income bracket and up to \$8,000 for those in the top bracket;
  - › Pay down around 70% of the Commonwealth’s fiscal deficit this financial year.
- › Our alternative approach for the **Child Care Subsidy** and **Parental Leave Pay** would see more support going to about 300,000 lower and middle income families, whilst saving about \$5 billion from families with income above \$180,000 per year, resulting in the loss of \$6,800 per year in support, on average.
- › Both programs are important for encouraging labour force participation and supporting outcomes for children, but these benefits tend to be much greater for lower and middle income families.
- › Our alternative approach to the **Age Pension** and **Aged Care** removes \$11.7 billion in support from the top 20% wealthiest households, and with a median reduction in benefits of \$30,000 in both programs. The change comes principally through fairer treatment of owner-occupied housing in assets tests.
- › We propose a policy innovation – the Retirement Contribution Scheme (ReCS), modelled on HECS – to ensure all retirees can opt-in to draw income at or above the full Age Pension rate, interest-free, against a range of financial assets to enable maintenance of a reasonable standard of living at at lower cost to taxpayers.

# \$21 billion in program savings could fund:



*These savings are also equivalent to the total program cost of the 2025-26 expenditure for:*

## JobSeeker



## Rent Assistance



## 2 Drifting away from equity

### 2.1 Australia's social safety net has been strong

The Australian notion of the 'fair go' expresses our concern for fairness, or equity. The policy expression of this ethos can be seen in our distribution of post-tax income, where Australia's measured inequality is around the OECD average. Our wealth distribution is less equitable than income, but far more equitable than that of the UK and the US.<sup>2</sup>

Our social support system includes universal health and education, and income payments for the least well off Australians.<sup>3</sup> Subsidised child care, Parental Leave Pay, Aged Care, the NDIS and the Age Pension are all part of this system.

Australia also has a relatively lower level of taxation compared with peer countries, meaning Australians pay less than taxpayers in other countries (Figure 1). A large part of this revenue is used to fund our social safety net.

The winning combination of a strong social safety net with a relatively lower tax burden has been possible historically in part because of our means testing approach that targets support toward those who need it most. Australia typically does this well in cash transfers, such as JobSeeker and Family Tax Benefits. These are highly targeted toward the bottom 20% of households that have the most financial need. On this measure, Australia fares better than almost every other country in the OECD.<sup>4</sup>

<sup>2</sup> OECD (2024). Household wealth is represented by the household's net worth. Net worth is calculated as the difference between the stock of household assets and the stock of household liabilities.

<sup>3</sup> Nwokora et al. (2024).

<sup>4</sup> OECD (2024). Australia has the third highest percentage behind Finland and the Netherlands.

FIGURE 1

### Australia fares well compared to our peers

Comparison to selected OECD countries, key indicators

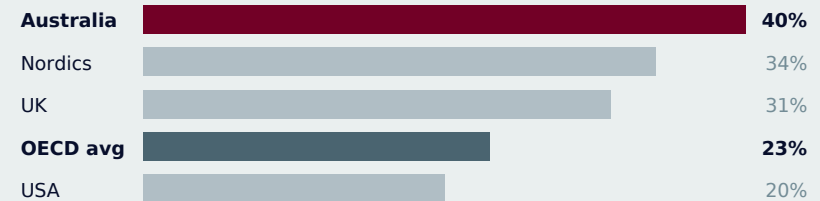
#### 01 Income equality near the OECD average

Disposable-income Gini · lower = fairer



#### 02 Highly targeted cash transfers to the least well off

Share to bottom 20%



#### 03 Funded with lower taxes than peers

Total tax · share of GDP



Note: All data is from 2020 to allow for comparability between countries. Nordic countries represent Norway, Sweden, Iceland, Finland and Denmark. The OECD average for the Gini coefficient, and for share of cash transfers to the bottom 20%, represents an unweighted average of OECD members.

Source: OECD (2025).

## 2.2 Who needs to access Australia’s safety net?

Distribution of means tested social transfers in Australia is based on an assessment of household need by income, and sometimes wealth. But how does financial need vary across Australian households?

Figure 2 illustrates the distribution of income and wealth in Australia. The distribution ranks households from lowest to highest in income and wealth, then splits the households into five groups (quintiles) that each represent 20% of the population. From this, we can estimate the median income and wealth — as well as the range — of each group.

The “middle” 20% of households have median pre-tax income of \$79,000 per year with a range of \$61,000 to \$103,000 (Figure 2). The median income of households in the top 20% is \$247,000 a year, over three times more than the middle group. The bottom 20% median income is \$21,000, about 1/4 of the middle group. The income of the top 20% of households is nearly 12 times that of the bottom 20%.

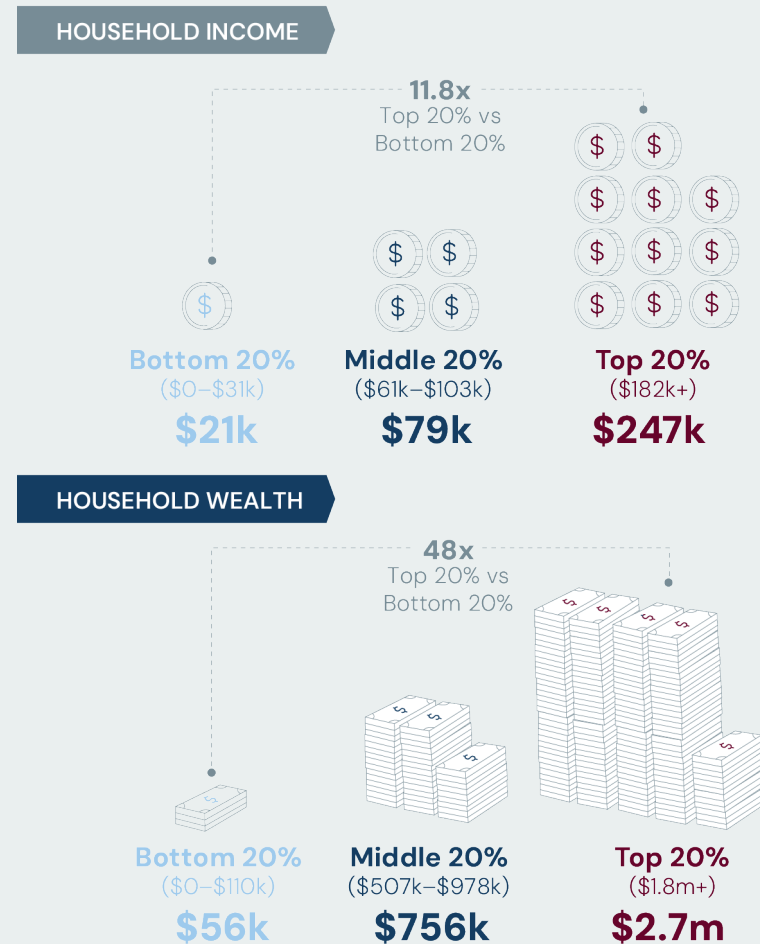
The wealth of the median household is \$756,000. The top 20% have median wealth of nearly four times that amount, or \$2.7 million. The median wealth of the top 20% is about 50 times the median wealth of the bottom 20%.<sup>5</sup>

High income and wealth often go together, but not always. Older Australians may sit in the top wealth quintile but with modest income. Younger high earners may have little wealth. This is important when considering how to best design Australia’s social safety net.

<sup>5</sup> Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

FIGURE 2

### The top 20% have much more than the middle and the bottom Household pre-tax income and wealth distribution, by quintile



Note: Quintiles segment households into five groups based on the distribution of income (top panel) and wealth (bottom panel). *Income* refers to pre-tax income and represents income before tax is taken out. We use the terms income and ‘pre-tax income’ interchangeably in text (and to mean the same thing as ‘taxable income’ and ‘ordinary income’). *Wealth* represents household net worth and represents the value of a household’s assets less the value of its liabilities. In our modelling we match the income and wealth definitions used for program eligibility as closely as possible (Appendix C).  
Source: Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

### 2.3 The growth of Australia’s social safety net

Australia’s social safety net comprises two kinds of ‘social transfers’. The government may provide *cash transfers*, untied, directly to recipients. Alternatively, the government may provide *in-kind transfers* by providing or subsidising services that are fully or partly funded by government.<sup>6</sup>

In-kind transfers have grown quickly (Figure 3).<sup>7</sup> Over the ten years to 2026–27, in-kind transfers are projected to rise by \$117 billion in real terms, a 62% increase, from 8.3% to 10.4% of GDP.<sup>8</sup> Cash transfers are projected to grow by \$14 billion in real terms, a 10% increase, but falling from 6.6% to 5.6% of GDP.<sup>9</sup>

Across Australia’s 11 million households, Commonwealth social transfers have grown by over \$6,000 per Australian household in real terms over a decade.<sup>10</sup> This is being driven by increased spending on healthcare (+\$34 billion), Aged Care (+\$22 billion) and the NDIS (+\$35 billion).<sup>11</sup>

Intergenerational Report projections suggest that health, Aged Care and the NDIS are expected to grow by \$500 billion in real terms, from 6.1% of GDP to 10.7% of GDP, over the next 40 years.<sup>12</sup>

<sup>6</sup> This can come from a government, not-for-profit or for-profit provider. Often, the recipient must pay part of the cost. The ‘in-kind’ value received refers to the amount funded by the government.

<sup>7</sup> Department of the Treasury (2017, 2026b).

<sup>8</sup> Policy Institute Australia analysis of Figure 3 and Australian Bureau of Statistics (2026).

<sup>9</sup> Ibid.

<sup>10</sup> Policy Institute Australia estimate using Australian Bureau of Statistics (2024) and Australian Bureau of Statistics (2016).

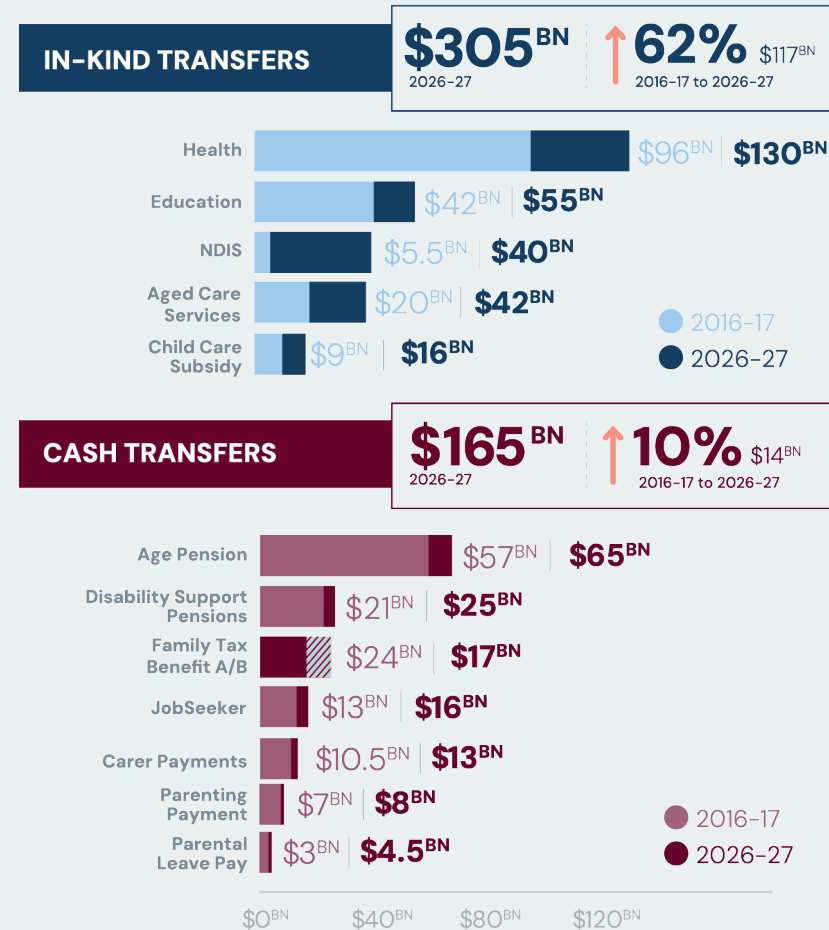
<sup>11</sup> The recent Commonwealth Budget outlined a \$37.8 billion reduction in projected NDIS payments over the forward estimates.

<sup>12</sup> Policy Institute Australia analysis of Department of the Treasury (2023), in \$2022–23. Note that this does not take into account policy changes since the Intergenerational Report was released.

FIGURE 3

#### In-kind transfers are the fastest growing social transfers

Commonwealth Budget expenditure, real \$2025



Note: All data has been converted into real \$2025. Figures exclude expenditure made by state and territory governments. Historical data may have small variations between publications depending on which data source is used. Child Care Subsidy reflects the Child Care Benefit plus Child Care Rebate before 2018. JobSeeker reflects Newstart Allowance prior to 2020. Aged Care Services include residential, flexible, home support and home care. NDIS includes just Commonwealth contributions, and also includes other disability expenditure that is not income support.

Source: Policy Institute Australia analysis of Commonwealth Budget and Portfolio Statements; Department of the Treasury (2017, 2026b); Department of Social Services (2017a, 2017b, 2026b); Department of Education and Training (2017); Department of Education (2026); Department of Health, Disability and Ageing (2026b); Australian Bureau of Statistics (2026).

## 2.4 Cash transfers are better targeted than in-kind transfers

Analysis of the share of benefits received by Australian households shows a very different pattern in the distribution of cash transfers versus in-kind transfers.

Cash transfers are often well targeted, with households in the bottom 20% of the income distribution receiving four times more than those in the top 20% (although several cash transfers are poorly targeted).<sup>13</sup>

Many in-kind transfers are not well targeted (Figure 4). An ABS analysis of a broad cross-section of in-kind transfers found that households in the bottom 20% of the *income* distribution actually receive *less* than those in the top 20% (around 80% as much). When looking at the *wealth* distribution, households all receive about the same average in-kind transfers, *regardless* of wealth.<sup>14</sup>

Some in-kind transfers are means tested (for example the Child Care Subsidy and Aged Care), but most are not. The NDIS, tertiary education, school education and public hospitals do not have means tests. As a result, many in-kind transfers go to people at the higher end of the income and/or wealth distribution.<sup>15</sup>

Given these distribution patterns, the relative growth of in-kind versus cash transfers means Australia’s social transfer system is becoming far less targeted — with more of the benefits going to the most well-off Australian households.

<sup>13</sup> Australian Bureau of Statistics (2018).

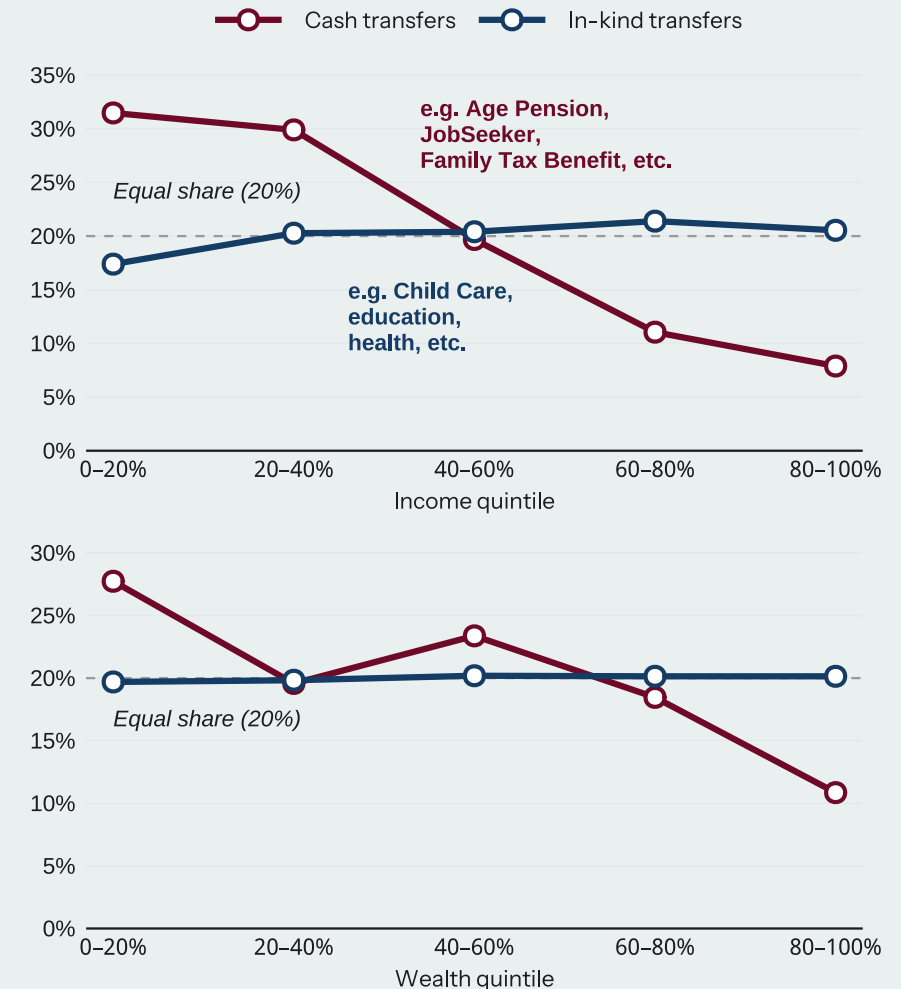
<sup>14</sup> Maltman et al. (2025) adopt a narrower definition of ‘in-kind transfers’ which excludes services provided directly by the government such as public hospital services, and find a greater degree of progressivity, but still less than cash transfers.

<sup>15</sup> Maltman et al. (2025).

FIGURE 4

### In-kind transfers are poorly targeted

Share of benefits received, per household, by income and wealth quintile, 2015–16



Note: This is data from 2015–16 which was the last year of publicly available and summarised data from the ABS. *Cash transfers* involve the government transferring cash, untied, directly to the recipient. *In-kind transfers* involve the recipient receiving services which are fully or partly funded by government. The ABS includes a broad cross-section of in-kind transfers including school and tertiary education; health including acute care, community health, pharmaceuticals, private health insurance rebates; child care assistance; and other social security and welfare benefits. Wealth and income are as defined in Figure 2.

Source: Australian Bureau of Statistics (2018).

## 2.5 Older Australians have been the main beneficiaries of the growth in social transfers

Older Australians have long been recipients of social transfers from the Commonwealth. The Commonwealth Age Pension was introduced in 1908, for example, and the Commonwealth has also been involved in Aged Care since the 1950s.<sup>16</sup>

Figure 5 illustrates how *per-adult* support provided to Australians from the Commonwealth has expanded over the past three decades.<sup>17</sup> Growth has occurred across age cohorts, although the increase has been lower for younger Australians compared to older Australians.

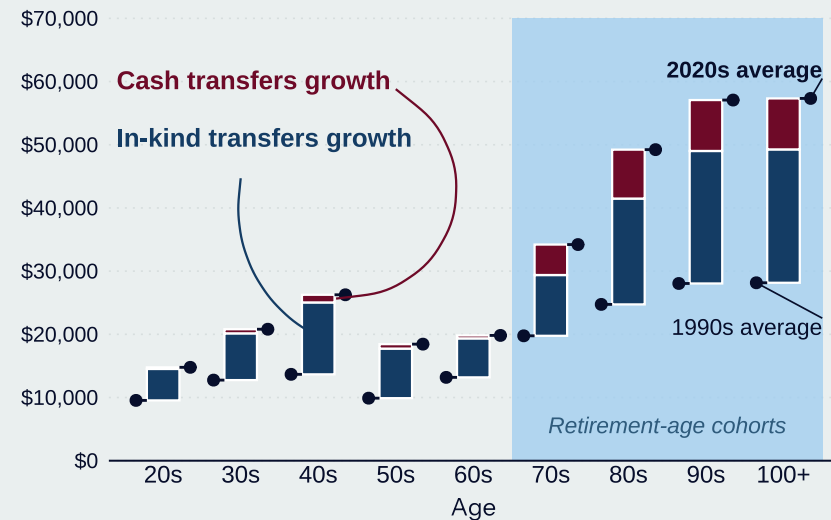
For example, for an Australian in their 40s, total social transfers have risen from around \$14,000 per capita in the 1990s to \$26,000 today, in real terms. This comprises an increase of \$11,000 for in-kind transfers and \$1,000 for cash transfers. The growth of in-kind transfers reflects an increase in child care subsidies, which were expanded materially from the early 1990s.

For an Australian in their 80s, social transfers have increased from around \$25,000 per capita in the 1990s to around \$50,000 today, in real terms. This has been mostly driven by increased spending on in-kind transfers, which have risen by \$17,000 (such as health and Aged Care) and, to a lesser extent, a rise in cash transfers, which have risen by \$8,000 (predominantly the Age Pension). Similar trends can be observed for Australians in their 70s, and those over 90.

FIGURE 5

### Older Australians have seen the largest increase in social transfers

*Benefits received, per adult, by age group, cash and in-kind, real \$2025*



Note: This reflects social transfers received by an individual, which can include social transfers from Commonwealth or state governments. 1990s average refers to 1993–94 to 1997–98. 2020s average refers to 2018–19 to 2022–23. Transfers for dependent children are assumed to flow to their parents.

Source: Varela et al. (2025).

<sup>16</sup> Department of the Treasury (2001); Department of the Prime Minister and Cabinet (2014).

<sup>17</sup> Varela et al. (2025). Buckley et al. (2026) point out that social transfers are one way the benefits of growth are shared throughout the community.

## 2.6 Rethinking means testing

This paper develops options to evolve Australia’s approach to means testing. We take the broad framework adopted by the Henry Tax Review as a starting point (Table 1) — with a particular focus on *equity* and *sustainability*.<sup>18</sup>

Within equity, we consider **vertical equity**, which means households with greater capacity to pay should contribute more, and households with greater need should receive more support. We target social transfers toward the bottom of the income or wealth distribution, while greatly reducing benefits to households in the top 20% of the income or wealth distribution.

We also consider **horizontal equity**, which means that households with similar financial capacity receive similar benefits. The vastly different treatment of household wealth based on asset type (namely owner-occupied housing versus other assets, outlined below in Section 3.3.1), is a prime example of this and one that is explored in depth in this report.

**Sustainability** underpins our approach. Sustainability means that social transfer programs can be sustained at their current level over time so that future cohorts can access similar levels of support to those receiving them today.

TABLE 1

### Henry Tax Review design principles of the tax and transfer system

PRINCIPLE	DESCRIPTION	EXAMPLE
<b>Equity</b>	Greater needs, greater support. Similar means, similar treatment — regardless of whether wealth is held as income, housing or super.	<i>Two couples with \$2m each — one in housing, one in super — receive very different pension entitlements.</i>
<b>Sustainability</b>	Fiscally affordable over time, so future cohorts can access support comparable to today.	<i>Social transfers are growing considerably as a share of GDP.</i>
<b>Simplicity</b>	Rules are easy to understand, administer and interact with.	<i>Pensioners shouldn’t need a financial adviser to model how downsizing affects them.</i>
<b>Efficiency</b>	Avoids distorting work, saving and housing decisions where it does not need to.	<i>Excluding the home from assets tests encourages retirees to hold more wealth in this way than they otherwise might.</i>
<b>Consistency</b>	Rules in one part of the tax and transfer system should not contradict rules or objectives in another.	<i>Differing treatment of owner-occupied housing in the Age Pension and Aged Care assets tests.</i>

Source: Policy Institute Australia analysis of Department of the Treasury (2010); Department of the Treasury (2023).

<sup>18</sup> Department of the Treasury (2010).

Improving the **simplicity** of transfer payments is largely beyond the scope of this report. However, recipients and their representatives regularly complain about the complexity of means tests for Aged Care and Age Pension in particular.<sup>19</sup> There is also evidence that early-stage retirees retain precautionary savings to mitigate the risk of the unknown cost of care as they age.<sup>20</sup> Simplifying the system may encourage more retired Australians to draw down on their savings (including superannuation) through retirement.

This complexity is partly structural. Social security payments are governed by several separate pieces of legislation,<sup>21</sup> which makes consistent means testing across programs difficult to achieve. Although reform of this kind falls outside this report, aligning the treatment of means tests across these Acts may support a more efficient system.

**Efficiency** relates to the quantum of taxes and transfers as well, the distortionary effect on behaviour, and the administrative burden (both time and cost) of complying with the tax and transfer system. Tax and transfer settings also act as powerful financial incentives that influence human behaviour. We examine these considerations, especially in relation to how working-age transfers such as Child Care Subsidy and Parental Leave Pay can influence decisions around workforce participation (Section 4.2.1 and Section 4.3.1). We also recognise that many Australian households will arrange their financial affairs to maximise their benefits across the tax and transfer system, including retirement incomes and estate planning.

Finally, we pull in the direction of greater **consistency** of means testing. This

is an important principle both across different programs and across time, as Australians make financial decisions based on their understanding of how the tax and transfer system will impact them over their lifetime. Sudden changes can be perceived as unfair to those who made decisions based on today's rules, even if the changes themselves work toward greater equity for all. Stability of policy settings is important, as is the consideration of any transitional arrangements when policy parameters are changed.

In addition to this framework, we also recognise that for some of these social transfers, **social outcomes** are important considerations in setting government policy. For the Child Care Subsidy, key goals include increasing workforce participation and providing benefits for children's early learning and development that comes from formal, approved child care. This is discussed in more detail in Section 4.2.3 and Section 4.2.4. For Parental Leave Pay, there are a number of social objectives, including promoting equality between men and women, encouraging women to continue to participate in the workforce, and increasing time off by fathers and partners. We discuss these in more detail in Section 4.3.3.

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<sup>19</sup> National Seniors Australia (2024); National Seniors Australia (2020).

<sup>20</sup> Daley, Coates, Wiltshire, et al. (2018).

<sup>21</sup> For example, the *Social Security Act 1991*; the *Aged Care Act 1997*.

## 3 Fairer means testing

### 3.1 Modelled changes to four transfer programs

We have developed alternative income and assets testing approaches for four major programs: the Age Pension, Aged Care, the Child Care Subsidy and Parental Leave Pay. Our model identifies the households that would be affected, and the funding impact of the changes.

We chose these four programs against the following criteria.

- **Size.** Each program is significant, with the four programs together accounting for around \$126 billion of expenditure in 2025–26.<sup>22</sup>
- **Existing means tests.** All four programs already have means testing arrangements, making them amenable to potential changes.
- **Loose existing targeting.** These programs are loosely targeted at present.
- **Data availability.** Each of these programs has sufficient data on the cohort involved for detailed modelling.

The list of programs for which we model alternative means tests is not intended to be exhaustive. There are other social transfers that are also not well targeted, and many — including most large in-kind programs — that are not means tested at all. The four programs modelled here are intended to demonstrate what a more equitable and sustainable means testing regime could look like, not to draw the boundary of where reform should start or stop.

<sup>22</sup> Department of the Treasury (2026b).

#### Box 1: Modelling approach

The Policy Institute Australia Microsimulation Model (PIAMM) has been developed for this project. It uses the HILDA dataset, which contains detailed information from annual interviews with around 10,000 households and 20,000 individuals.<sup>a</sup> People living in Residential Aged Care are not adequately represented in HILDA's household-based sample, so we have had to model the likelihood of entry into Aged Care for older Australians (a common approach).<sup>b</sup>

PIAMM includes all key personal income tax and transfer policies, and maps policy changes onto each individual and household in the model, which are weighted to provide estimates of distributional and fiscal effects for Australia. PIAMM is calibrated to 2025–26 and all results are in 2025–26 dollars. The results therefore estimate the potential impact for this current financial year only. There are no forward projections.

PIAMM doesn't attempt to estimate 'behavioural' responses to policy changes. For example, it assumes that people are not changing how much they work in response to modelled changes in the Child Care Subsidy. Instead, we address these issues through our analysis of workforce disincentive rates (which are mostly similar) and review of the literature (which suggests the labour response is modest) (Section 4). Behavioural models require assumptions about how people respond to policy changes. Further detail on PIAMM is in Appendix C.

<sup>a</sup> Melbourne Institute (2025). The ABS has the only similar Australian dataset, the Survey of Income and Housing, but the latest data is from 2018–19.

<sup>b</sup> Nepal et al. (2011); Abello et al. (2008).

### 3.2 Current state: income means tests

Income means tests are used for most cash transfers and some in-kind transfers to determine whether an individual or household is eligible, and often what level of support they can receive. They are typically tested against pre-tax income, although different definitions are used.<sup>23</sup>

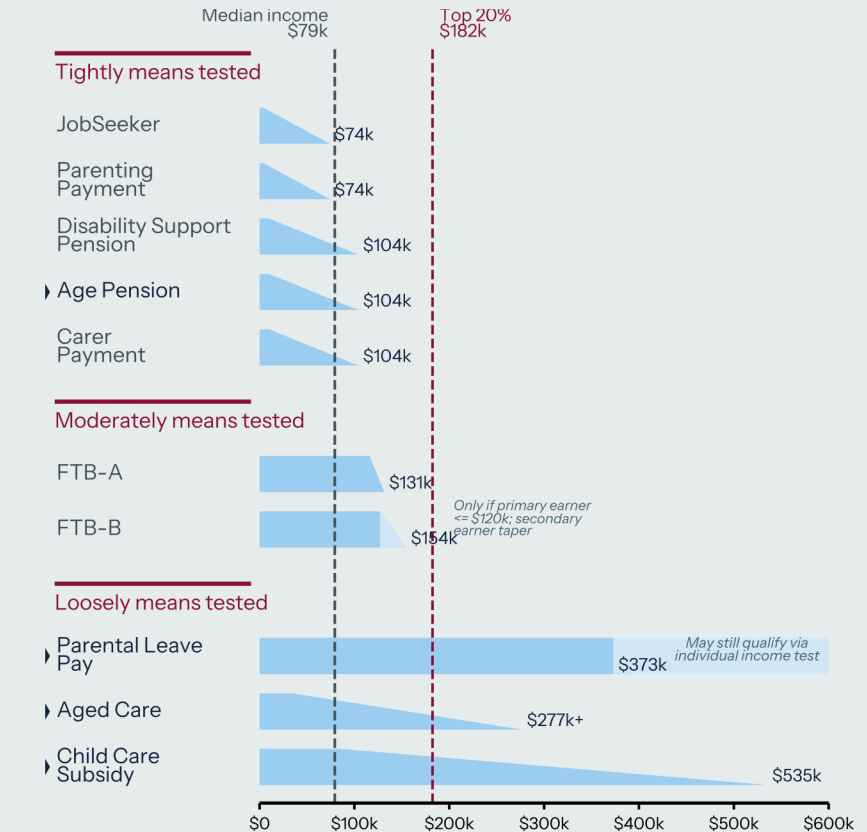
Cash transfers are typically income tested with low thresholds and steep taper rates. As shown in Figure 6, JobSeeker and the Parenting Payment taper off before the median income of \$79,000. The Disability Support Pension, the Age Pension, Carer Payment and Family Tax Benefit A and B have more generous income tests, tapering off before the top 20% – at between \$104,000 and \$154,000. Aged Care extends support to the top 20% income-earning households.<sup>24</sup>

The Child Care Subsidy and Parental Leave Pay are more generously applied – less than 1% of households have incomes that would make them ineligible for both the Child Care Subsidy and Parental Leave Pay.<sup>25</sup>

FIGURE 6

#### Parental Leave Pay and the Child Care Subsidy have generous income tests

*Income test, share of maximum benefit available, annual pre-tax income, selected working-age social transfers*



Note: This chart is illustrative only for a partnered Australian family who is eligible to receive various Commonwealth government social transfers. As an example, if the data shows 100% at \$50,000, that means a household earning \$50,000 of pre-tax income per year is eligible to receive the full (i.e. 100%) entitlement of that benefit. Note that this analysis assumes that each household meets the asset test and other eligibility criteria. Family Tax Benefit A assumes two dependent children to calculate the maximum income threshold. Source: Services Australia (2026b); Melbourne Institute (2025).

<sup>23</sup> We use the term income and 'pre-tax income' interchangeably in text (and to mean the same thing as 'taxable income' and 'ordinary income'), but in our modelling we have matched the definitions used in determining program eligibility as closely as possible (Appendix C). Pre-tax income is a decent proxy for the true means of a household. However, individuals with similar pre-tax incomes can face very different effective tax rates, due to different features in the tax system, such as the discount for capital gains (Kaplan et al., 2025).

<sup>24</sup> Services Australia (2026b).

<sup>25</sup> Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

### 3.2.1 Child Care Subsidy and Parental Leave Pay are available to very high income households

The **Child Care Subsidy** has the highest household income cut off of any means tested Commonwealth payment, with support available to families with combined pre-tax income up to \$535,279.<sup>26</sup> Some families in the top 2% of all income earning households are eligible for support.<sup>27</sup> A family with combined income of \$400,000 (putting them in the top 4%) and two children in care five days per week is eligible for a 27% subsidy, worth about \$21,000 a year.<sup>28</sup>

Because of this, and because among families with preschool-aged children those in the top income 20% are about twice as likely to use formal child care as those in the bottom 20%, we find that *most* of the benefit from the Child Care Subsidy goes to households in the top 40% of the income distribution.<sup>29</sup>

Child Care Subsidy means testing was loosened under changes in 2023 that extended the highest cut-off for total household income from \$357,000 to around \$530,000. A per-child annual subsidy cap of \$10,655 for families with pre-tax income above \$190,000 was also removed.<sup>30</sup> A family with pre-tax income of \$250,000 and two children in child care five days a week would be eligible for around \$52,000 a year in Child Care Subsidy following these changes.<sup>31</sup>

<sup>26</sup> Services Australia (2026f).

<sup>27</sup> Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

<sup>28</sup> Assumes provider charges at or above cap rate of \$14.63 per hour and 100 hours of care. Policy Institute Australia estimate using Services Australia (2026d).

<sup>29</sup> Policy Institute Australia Microsimulation Model (PIAMM).

<sup>30</sup> Parliament of Australia (2021).

<sup>31</sup> Policy Institute Australia estimate using Services Australia (2026d), assumes both children are under 5 and receive 100 hours of care per fortnight at cap rate.

**Parental Leave Pay** is paid for up to 120 days (or 24 weeks based on a five-day work week) at the national minimum wage (\$948 per week pre-tax), meaning that in total it is worth up to \$22,754.<sup>32</sup> It is only available to new parents who are in regular paid work prior to the arrival of the child.<sup>33</sup>

The full benefit is available to families (including single parent families) that had a combined pre-tax income of up to \$373,094 in the year before the child's arrival. However, families with combined pre-tax income *above* \$373,094 are eligible for about 90% of the benefit (21 out of 24 weeks) if one parent had individual pre-tax income below \$180,007.<sup>34</sup>

Only 3% of otherwise eligible households are ineligible for the *full* benefit due to income exceeding the household threshold. And only about one-third of these households would fail to meet the individual income test. In other words, despite the appearance of means testing, just 1% of otherwise eligible households would fail all income tests for Parental Leave Pay.

In addition to taxpayer-funded Parental Leave Pay, more than 70% of workers that are in the top 50% of income earners have access to employer-provided paid parental leave, typically paid at their wage.<sup>35</sup> A parent with a pre-tax wage of \$180,000 a year who is eligible for 6 months of employer-funded paid parental leave would be eligible for the government-funded benefit of around \$20,000,<sup>36</sup> *in addition* to their employer-funded benefit of \$90,000, even if their partner earned half a million dollars a year or more.

<sup>32</sup> For babies born from 1 July 2026, the benefit is legislated to increase to 130 days (equivalent to \$24,650 using 2025–26 rates), with at least 20 days reserved for the second parent.

<sup>33</sup> At least 330 hours total across 10 of the prior 13 months (roughly one day per week on average).

<sup>34</sup> Thresholds are indexed to CPI.

<sup>35</sup> Australian Bureau of Statistics (2025b).

<sup>36</sup> 21 weeks at \$948 per week.

### 3.3 Current state: assets means tests

Assets means tests use the net value of an individual’s or household’s assets (net of any liabilities such as a home loan) to determine whether an individual or household is eligible, and often what level of support they can receive. They are less common than income tests – applying to payments under the *Social Security Act 1991* (Cth), but rarely to other cash or in-kind transfers. When they are applied, asset classes are not treated consistently. Most notably, special treatment of owner-occupied housing means some of Australia’s wealthiest households receive generous government benefits.

As shown in Figure 7, JobSeeker and the Parenting Payment have strict assets tests, cutting off at around \$740,000 in assessable assets.<sup>37</sup> The cutoff is just below median household wealth of \$756,000.

Some social transfers including the Child Care Subsidy, Parental Leave Pay and Family Tax Benefit A and B, have *no* assets test. For Family Tax Benefit A and B, the absence of an asset test is relatively inconsequential given its income test thresholds. But for the Child Care Subsidy and Parental Leave Pay, which have loose income testing, families with very high wealth can get substantial support. We estimate that about 10% of families receiving the Child Care Subsidy, and about 5% of families receiving Parental Leave Pay, have wealth above \$1.5 million.<sup>38</sup> Sitting between transfers with strict assets tests, and those with none, are programs such as the Age Pension and parts of Aged Care, with assets test allowing for substantial support above household median wealth.

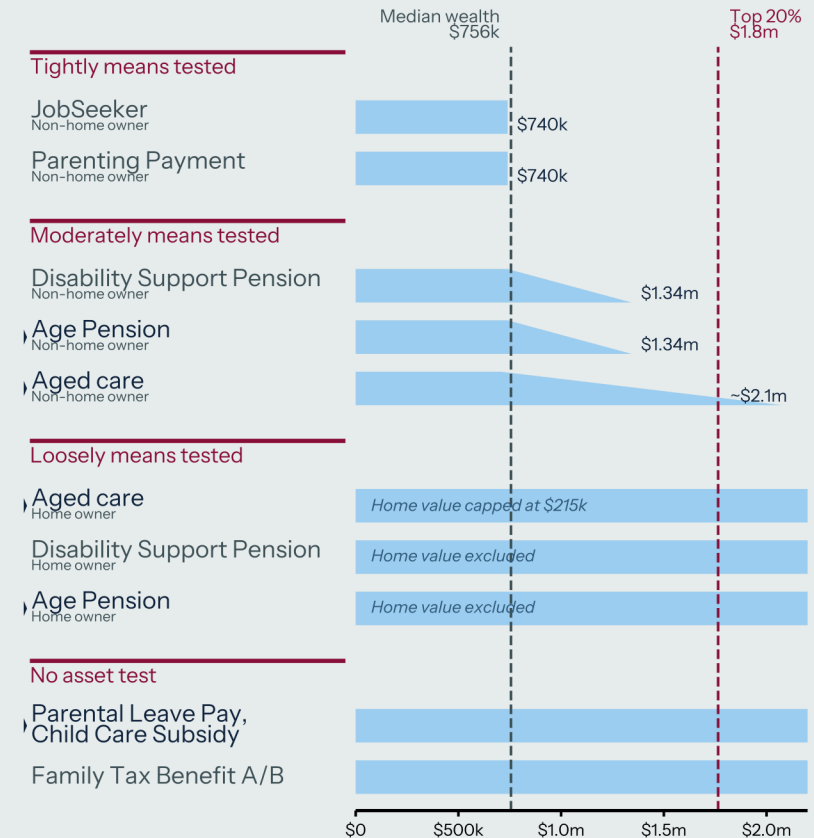
<sup>37</sup> ‘Assessable assets’ simply means the assets that are assessed in a means test. For example, if owner-occupied housing is not assessable, then its value is not included in the total value of someone’s assets.

<sup>38</sup> Not including superannuation.

FIGURE 7

#### Aged Care and the Age Pension have generous asset tests, particularly in treatment of owner-occupied housing

Asset test, share of maximum benefits available, wealth



Note: The analysis for this figure assumes that each household meets the income test and other eligibility criteria. For homeowners, the value of all assets are assumed to be in owner-occupied housing, and for non-homeowners, the value of all assets is assumed to be in other assets.

Source: Services Australia (2026b).

### 3.3.1 Preferential treatment of owner-occupied housing

It is often stated that a retiree's home is not counted in means testing for entitlements to the Age Pension or Aged Care, but that is not correct.

Under the *Social Security Act 1991* (Cth), the value of an Age Pension recipient's 'principal home' is technically *not* counted in calculating the value of a person's assets. However, a retiree's status as being either a homeowner or a renter results in variation to the assets test that is applied to them. Non-homeowners can have up to \$258,000 more in assets outside the family home than homeowners before their pension entitlement is reduced. This is true for both singles and couples.<sup>39</sup>

Effectively, this means that all owner-occupied housing is valued at \$258,000 when eligibility for a full or part pension is calculated.

For Residential Aged Care, owner-occupied housing can be included in the assets test up to a capped amount of \$214,884. For couples, each partner is considered to own half of the home, so the capped amount of \$214,884, or half the net market value of the house (if lower), is included in the means assessment for any partner in Residential Aged Care.<sup>40</sup> If the home is occupied by a 'protected person', such as the care recipient's partner, it is excluded entirely.

<sup>39</sup> Services Australia (2026b).

<sup>40</sup> Department of Health, Disability and Ageing (2026a). Many people moving into Residential Aged Care will sell their home and put their money into a Refundable Accommodation Deposit (RAD) or Refundable Accommodation Contribution (RAC). One incentive for doing this is that the RAD/RAC is excluded from the assets test for the Age Pension, while the value of the home is *included* if it is unoccupied for more than two years.

#### Box 2: The Age Pension, Residential Aged Care and Support at Home

The **Age Pension** is a cash transfer for people aged 67 and over. Eligibility is based on household income and assets, with the full pension worth about \$31,200 a year for singles, and \$47,100 a year for couples in 2025–26. Currently, there are about 2.7 million pension recipients across about 2 million households.

**Residential Aged Care** provides accommodation and 24-hour care for older Australians with high care needs. Around 198,000 people were using permanent or respite residential care at 30 June 2024.<sup>a</sup> In 2025–26, Residential Aged Care accounted for about \$26 billion of annual Commonwealth expenditure<sup>b</sup>. The median length of stay for permanent residential care is 19 months,<sup>c</sup> and average Commonwealth expenditure per resident-year is roughly \$130,000, with an average private contribution of \$35,000, typically funded in part by the pass through of the Age Pension.

Aged Care **Support at Home** provides in-home support for older Australians who need help to live independently.<sup>d</sup> Support at Home currently supports about 380,000 people and is estimated to cost about \$6.5 billion in 2025–26, with an average government subsidy per recipient of about \$17,000.<sup>e</sup>

<sup>a</sup> Australian Institute of Health and Welfare (2025b).

<sup>b</sup> Department of the Treasury (2026b).

<sup>c</sup> Australian Institute of Health and Welfare (2025b).

<sup>d</sup> The Commonwealth Home Support Programme (CHSP) provides entry-level support at home, but has no government means testing and is to fold into Support at Home, so is not our focus (although it is included in our modelling).

<sup>e</sup> Department of Health, Disability and Ageing (2026b).

For Aged Care 'Support at Home', means testing is based partly on eligibility for a full or part pension, in which the value of the home is effectively capped, as described above. However, it is also based on eligibility for the Commonwealth Seniors Health Card, and both this and the exact contributions for part pensioners or self-funded CSHC holders are based on means tests which exclude owner-occupied housing.

The upshot of these complicated rules is that a retiree household with a home worth \$500,000 and one with a home worth \$5 million are treated identically, despite very different means. And both tend to be treated much more favourably than non-homeowners with the same wealth in other assets such as shares or super.

This "one size fits all" treatment of owner-occupied home values creates horizontal inequity between retirees who hold their wealth in housing and those who hold it in other forms. Consider two single retirees, each with total net worth of \$1.5 million:

- John owns a home worth \$1.2 million and has \$300,000 in financial assets. His assessable assets are \$300,000, and he is eligible for a full pension.
- Carol has sold her home to relocate near her grandchildren, rents, and holds \$1.5 million in superannuation and investments. Her assessable assets are \$1.5 million, so she receives no pension.

Both retirees have similar capacity to fund their own retirement, but one receives \$31,200 per year in taxpayer-funded support and the other receives nothing.<sup>41</sup>

An example from Aged Care: Agnes is an Aged Care resident who has just

<sup>41</sup> Inclusive of Pension Supplement and Energy Supplement.

moved out of her \$3 million home, where her husband Arthur still lives. The home is excluded entirely from the Residential Aged Care assets test. Beryl and her husband Bob are in a similar situation, but are renters and have \$3 million in shares and super. Agnes and Beryl are in the same Aged Care facility receiving the same care at the same overall cost. Agnes receives government support of approximately \$149,400 a year, and Beryl gets about \$76,000.<sup>42</sup>

The primary rationale for special treatment of owner-occupied housing in assets tests is the difficulty in drawing income from the home as an asset. We propose a solution to this issue in Section 5.2.

The strongly preferential treatment of the owner-occupied home acts as a disincentive for older Australians to sell their home and move, including downsizing. If a pensioner sells a \$1.5 million home and moves to a \$700,000 home, the \$800,000 in sale proceeds becomes a financial asset that is counted in the means test, substantially reducing or eliminating their pension. The system instead incentivises retirees to remain in a home that may be larger than needed, potentially reducing housing turnover.<sup>43</sup>

### 3.3.2 Many high wealth households receive the Age Pension or substantial Aged Care contributions

The preferential treatment of owner-occupied housing means that many wealthy households receive the Age Pension, as well as significant contributions

<sup>42</sup> Assumes both residents receive care at the modelled average residential aged-care cost in the same facility (Appendix C).

<sup>43</sup> National Seniors Australia (2014). The Government has introduced some measures to partially address this disincentive, including the downsizer contribution to superannuation (Australian Taxation Office, 2026), and an assets test exemption for proceeds from downsizing for up to 24 months (Services Australia, 2026e). However, these measures only partially offset the underlying incentive to retain a high-value home.

to their Aged Care costs.

About 12% of households receiving the Age Pension are in the top 20% of Australian households by wealth — holding wealth of at least \$1.8 million.<sup>44</sup>

This wealth is mostly held in owner-occupied housing.

A retiree couple with a \$5 million house in Sydney but with few other assets would be among the wealthiest 3% of households in Australia. Nonetheless, they would be eligible for a full Age Pension worth \$47,100 a year, and up to about \$150,000 a year in additional support if one of them moves into Residential Aged Care.<sup>45</sup>

Research shows that wealthier retirees tend to have low asset draw-down rates over retirement, with many holding more wealth at death than they did at age 67.<sup>46</sup> For some retirees, this may be explained by precautionary saving — meaning the practice of deliberately restraining spending and retaining assets in the early stages of retirement to ensure they can afford higher quality, more expensive care as they age if that is what is required.<sup>47</sup>

Non-homeowner households with high levels of wealth can also receive support that appears out of line with current need, even if their need for support increases as their assets reduce through retirement. A couple aged 89 and 90 who rent, but have \$1.3 million of other assets (for example, superannuation

<sup>44</sup> Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

<sup>45</sup> Services Australia (2026c); Department of Health, Disability and Ageing (2025).

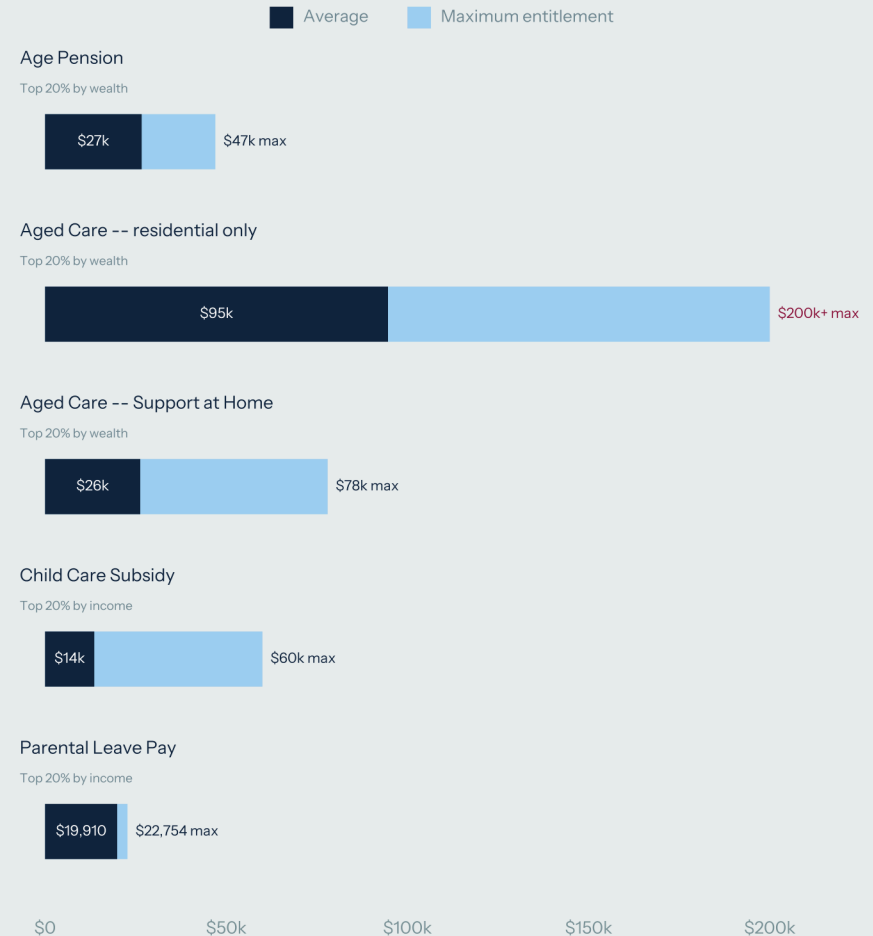
<sup>46</sup> Daley, Coates, Wiltshire, et al. (2018); Department of the Treasury (2020).

<sup>47</sup> Department of the Treasury (2020).

FIGURE 8

**The top 20% of households by wealth or income can receive substantial social transfers**

*Average and maximum annual payment to top 20% households, by pre-tax income and wealth, selected social transfers*



Note: Top 20% defined by wealth (Age Pension, Aged Care) or income (Child Care Subsidy, Parental Leave Pay). Average payments are typical annual amounts for top quintile recipients. Residential Aged Care maximums can exceed \$200,000 annually for regional areas with acute care needs. Child Care Subsidy maximum assumes \$182,000 household income with two children in five-day care.

Source: Policy Institute Australia analysis; Services Australia (2026b); Department of Health, Disability and Ageing (2026a).

or cash in the bank) would receive a part pension. It is important to note that the pension benefit available evolves as a household's means evolve. A household with assets that can be used to support their retirement will become eligible for higher pension benefits as these assets are drawn down.

### 3.3.3 Caps on contributions in Aged Care primarily benefit the wealthy

The extent to which even very wealthy households contribute to their own costs in the Aged Care system is limited by caps on private contributions. Changes that commenced 1 November 2025,<sup>48</sup> now carve out 'clinical care' — meaning nursing and allied health support (but not including care from a doctor)<sup>49</sup> — from private contribution. All clinical care is fully government-funded both for Residential Aged Care and for Support at Home.<sup>50</sup>

The rationale underlying the change is that clinical care would be free for recipients if they received it through the public health system, such as in a public hospital. While this is true, caps such as this have the effect of significantly curtailing the contributions from households with ample capacity to contribute more. Indeed, our modelling finds that with these caps in place, other means testing changes such as to treatment of owner-occupied housing have minimal effect on the overall contributions made by the wealthiest recipient households.

*Lifetime* caps on private contributions also apply. For those entering the Aged Care system after 1 November 2025, a lifetime cap of \$137,917 applies for

<sup>48</sup> With some grandfathering of arrangements (Services Australia, 2026a).

<sup>49</sup> Care provided by a GP or specialist doctor is not included in the Aged Care definition of 'clinical care' as it is not funded through the Aged Care system.

<sup>50</sup> As part of the 2026 Budget, Health Minister Mark Butler announced that showering and other personal care services would be reclassified as 'clinical care' (Butler, 2026).

non-clinical care contributions across Support at Home and Residential Aged Care.<sup>51</sup> The primary beneficiaries of this rule are those with greater means, where private contributions will be made only up to this cap.

<sup>51</sup> The non-clinical care contribution also stops after 4 cumulative years of paying it, even if the dollar cap has not been reached. Previous cap arrangements have been grandfathered.

## 4 Reform options for fairer means testing

### 4.1 A direction for reform

We have developed alternative income and asset means tests to better target Australia's social transfers, and modelled the impact of the change on households. The objective is to improve vertical and horizontal equity in the programs by reducing support for the most well-off households in Australia, thereby also preserving program sustainability.

We focused on four programs — the Child Care Subsidy, Parental Leave Pay, the Age Pension, and Aged Care — which were selected based on their size, relatively poorly targeted means testing regimes, and data availability.

This section presents the results of our four 'preferred options' to existing means testing approaches. This paper does not aim to design the definitive means testing arrangements for any of the programs, but rather to identify opportunities for meaningful reform.

Table 2 provides an overview of these four preferred options. Effectively, the Child Care Subsidy and Parental Leave Pay have been modelled with stricter income tests that exclude high income households. The Age Pension and Aged Care have been modelled with a means test that more fairly accounts for the value of owner-occupied housing. The sections below detail the impact that these changes would make relative to current means testing arrangements, and the estimated distributional and fiscal effects. Alternative options are also presented.

TABLE 2

### Our preferred options for better targeting four programs

PROGRAM	SUMMARY OF PREFERRED OPTIONS MODELLED
<b>Child Care Subsidy</b>	<ul style="list-style-type: none"> <li>Increase support at low and middle incomes, but taper payments out earlier: <b>95%</b> subsidy up to <b>\$133,000</b>, phasing to zero by <b>\$250,000</b>.</li> <li>Higher threshold for the <b>95%</b> subsidy for a second child up to <b>\$250,000</b>, phasing to zero by <b>\$400,000</b>.</li> <li>See Section 4.2.1 for more details.</li> </ul>
<b>Parental Leave Pay</b>	<ul style="list-style-type: none"> <li>Tighten eligibility by reducing the family income threshold from <b>\$373,000</b> to <b>\$200,000</b>.</li> <li>Remove the secondary individual-income test.</li> <li>See Section 4.3.1 for more details.</li> </ul>
<b>Age Pension</b>	<ul style="list-style-type: none"> <li>Lift the asset test thresholds for homeowners by <b>\$258,000</b> to match non-homeowners.</li> <li>Include the value of equity in any owner-occupied housing that is above <b>\$500,000</b> in the assets test.</li> <li>See Section 4.4.1 for more details.</li> </ul>
<b>Aged Care</b>	<ul style="list-style-type: none"> <li>Include the value of equity in any owner-occupied housing that is above <b>\$500,000</b> in the means tests.</li> <li>Remove exemptions when the home is occupied.</li> <li>Increase private contributions for those with substantial means, and reduce contributions for some with less means.</li> <li>See Section 4.5.1 for more details.</li> </ul>

Note: These changes to the Age Pension assets test would have flow-on impacts for recipients of some other social transfers. For example, Support at Home payments are determined by pension status and eligibility — these interactions are accounted for in our modelling (see Appendix C).

### Box 3: How should owner-occupied housing be treated?

In principle, including the full value of owner-occupied housing is the most equitable way to treat wealth in means testing. This is because every dollar of equity in owner-occupied housing would be treated the same as other assets, such as superannuation, investment properties, or shares. But this approach would affect a large number of retiree homeowners, including some with modest homes, and would be extremely challenging politically.

Instead, we propose including the value of equity in any owner-occupied housing that is above \$500,000. We do this for several reasons. First, it ensures that anyone who owns a home worth a bit more than \$1 million (and with limited other assets) would still receive the full Age Pension and maintain Aged Care Support at Home entitlements. This is above both the median value of an Australian dwelling of \$930,000 and the median value of a capital city dwelling of \$1.0 million.<sup>a</sup> Second, it limits the number of people that are affected. For example, under our proposed change, for the Age Pension, around 80% of full pensioners would continue to receive the full pension.

Policymakers could also consider a higher threshold, although a higher threshold saves less, and does less to address the horizontal inequity between homeowners and non-homeowners with similar total wealth. One option would be to phase in such a change by setting a higher threshold such as \$1 million but with this value fixed in nominal terms, so that it captures a greater proportion of home equity over time.

<sup>a</sup> Cotality (2026).

We have also modelled including the value of equity in any owner-occupied housing that is above \$1 million. Results for both this higher threshold, and full inclusion of owner-occupied housing, are presented in Table 7 and Table 9 below.

Other reviews have proposed similar approaches. The *2010 Henry Tax Review* proposed that, to increase the fairness of the means test, a cap should be applied to the owner-occupied housing exemption, with a cap of around \$1.2 million, and with any value above that counting in the Age Pension means test.<sup>a</sup> The *National Commission of Audit* also proposed a cap for the exemption, with different thresholds for couples (\$750,000) and for singles (\$500,000).<sup>b</sup>

The *Productivity Commission* has noted that, in principle, the best policy response is to *fully remove* the exemption and include the entire value of owner-occupied housing in a new means test for the Age Pension.<sup>c</sup> They have also previously argued that for Residential Aged Care “the relevant share of a person’s former principal residence should be included in the total assets test”.<sup>d</sup> *Grattan Institute* have advocated for including owner-occupied housing in the means test for both the Age Pension and Aged Care, above a threshold of \$500,000.<sup>e</sup>

<sup>a</sup> Department of the Treasury (2010).

<sup>b</sup> National Commission of Audit (2014).

<sup>c</sup> Productivity Commission (2015).

<sup>d</sup> Productivity Commission (2011b).

<sup>e</sup> Daley, Coates, Wiltshire, et al. (2018); Daley, Coates, and Wiltshire (2018).

#### 4.1.1 Reform results in substantial savings

Our preferred options across the four programs would reduce expenditure on these four programs by about \$21 billion, or 17% of the total expenditure in 2025–26 (Figure 9).<sup>52</sup> The reduction primarily comes from households in the top 20% of income or wealth distribution, who receive \$25.6 billion in support across the four programs, around 20% of total program expenditure.<sup>53</sup>

The most significant impact comes through stricter application of the assets test in the Age Pension and Aged Care programs — with savings of around \$16 billion. The savings from Parental Leave Pay and the Child Care Subsidy are more modest, at around \$5 billion, reflecting the smaller scale of the two programs.

These cost savings improve program sustainability — by reducing the call on taxpayers to fund support today, and by helping to ensure future governments will have sufficient capacity to retain entitlements for those in need long into the future.

Freed up funds could of course be used for other priorities. This paper does not recommend how \$21 billion in savings could be deployed, but the magnitude is significant. To illustrate, \$21 billion in savings is sufficient to:

- Cut the tax rate for all income tax thresholds by 1.7 percentage points, which would reduce personal income taxes by up to \$2,000 for Australians in the middle income bracket and up to \$8,000 for those in the top bracket.
- Provide close to \$5,000 each year in benefits to each of the 4.4 million

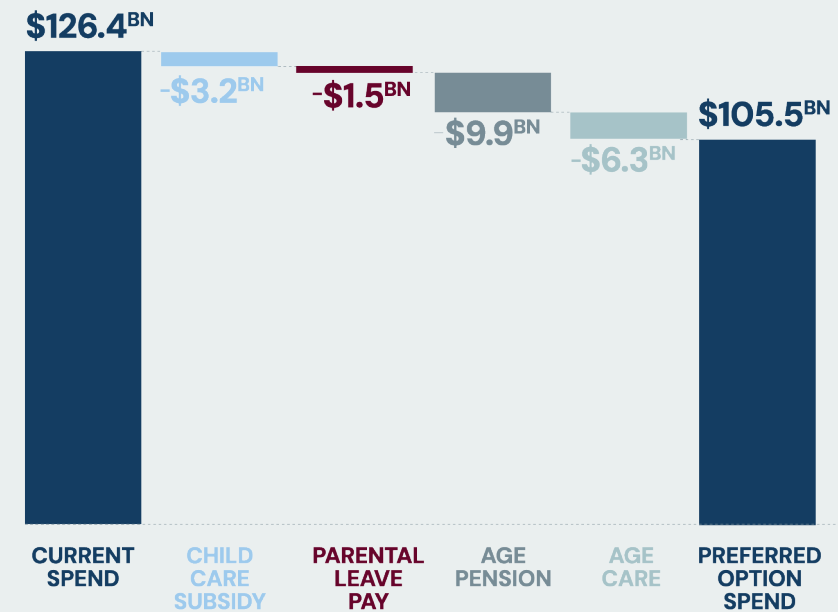
<sup>52</sup> Estimate is for 2025–26. Our model does not include forward projections.

<sup>53</sup> For 2025–26, we estimate \$9.6b went to the top 20% by income for Child Care Subsidy, Parental Leave Pay; \$16b went to the top 20% by wealth for Age Pension, Aged Care.

FIGURE 9

#### Reform could save around \$21 billion a year

Current program spend and modelled savings, 2025–26



Source: Policy Institute Australia Microsimulation Model (PIAMM); Department of the Treasury (2026a).

households in the bottom 40% of households by income or wealth.<sup>54</sup>

- Fund meaningful increases in supports targeting those most in need — in 2025–26, total expenditure on JobSeeker was \$16 billion and on Rent Assistance it was \$7 billion.<sup>55</sup>
- Pay down around 70% of the Commonwealth’s current year fiscal deficit.

<sup>54</sup> Policy Institute Australia estimates based on Australian Bureau of Statistics (2024); Department of the Treasury (2026a); Parliamentary Budget Office (2026).

<sup>55</sup> Department of Social Services (2026b).

### 4.1.2 Reform would better target support

Overall, our preferred reform options improve vertical equity through reducing benefits to Australia’s most well off households.

Figure 10 shows the combined savings by *income quintile* for the Child Care Subsidy and Parental Leave Pay, and by *wealth quintile* for the Age Pension and Aged Care. Here and throughout the report, distributions are presented for the population, not for those receiving a particular benefit.

For the Child Care Subsidy and Parental Leave Pay, income is most relevant, as recipients are typically families with working-age parents. Almost all savings – about \$5 billion – comes from the top of the income distribution. For parents receiving Parental Leave Pay, the change would result in the highest income families losing payments worth up to \$22,754 per child. For the Child Care Subsidy, just over 500,000 families in the top 20% of the income distribution would see a reduction in the benefit they receive of about \$6,800 a year on average under our approach.

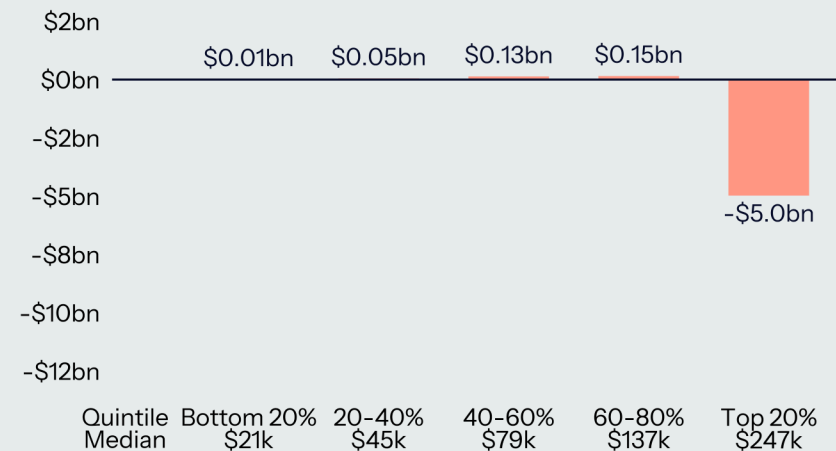
For the Age Pension and Aged Care, wealth is most relevant, as recipients are typically retired. About \$12 billion in savings comes from the top 20% wealthiest Australian households, with a further \$5 billion from those in the 60–80% quintile.

The sections below provide more detail on our preferred reform options. This includes how many people may be affected at each part of the income or wealth distribution, how average payments per group change, and how those changes are distributed across the population.

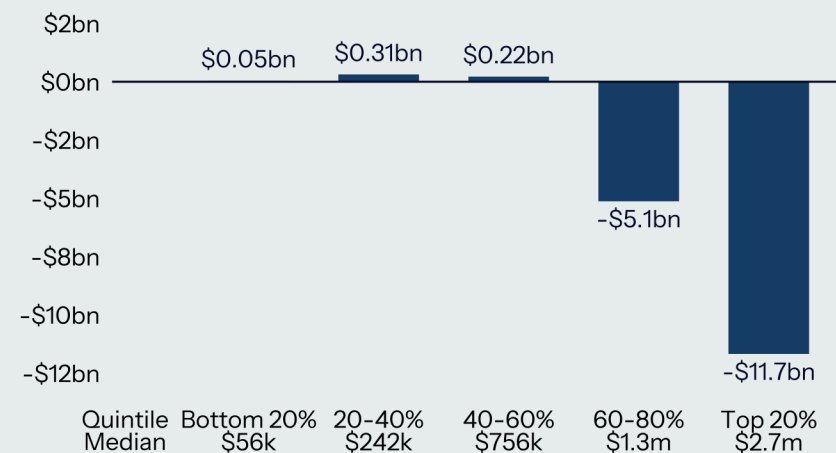
FIGURE 10

### The lion’s share of the savings comes from the top 20% of the income or wealth distribution

*Change in payments by income quintile, under preferred options for Child Care Subsidy and Parental Leave Pay*



*Change in payments by wealth quintile, under preferred options for Age Pension and Aged Care*



Source: Policy Institute Australia Microsimulation Model (PIAMM).

## 4.2 Better targeting the Child Care Subsidy

### 4.2.1 A tighter income test, with more support for low and middle income families

The Child Care Subsidy reduces the out-of-pocket cost of approved child care. In December quarter 2025, the Child Care Subsidy was provided for 1.4 million children from 1.0 million families.<sup>56</sup> Families with very high incomes of up to \$535,000 a year are eligible for the Child Care Subsidy.

Our 'preferred option' better targets the Child Care Subsidy, while minimising a potential change in financial incentives for parents to remain in paid work.

- It lifts the standard Child Care Subsidy rate from 90% to 95% for the first child of families with income up to \$133,000, which increases support (and reduces a barrier to work) for families more in need.
- It tightens the income test at the top, so that the standard subsidy for the first child falls to 0% when family income reaches \$250,000, down from \$535,000 at present.
- It lifts the threshold for second and younger children, so that the higher subsidy remains at 95% up to \$250,000 before falling to 0% when income reaches \$400,000. This novel structure separates the phase out for first and second child rates to minimise the disincentive to work associated with child care where it is strongest – for families with two kids in care.<sup>57</sup>

Figure 11 compares our preferred option and the current income test.

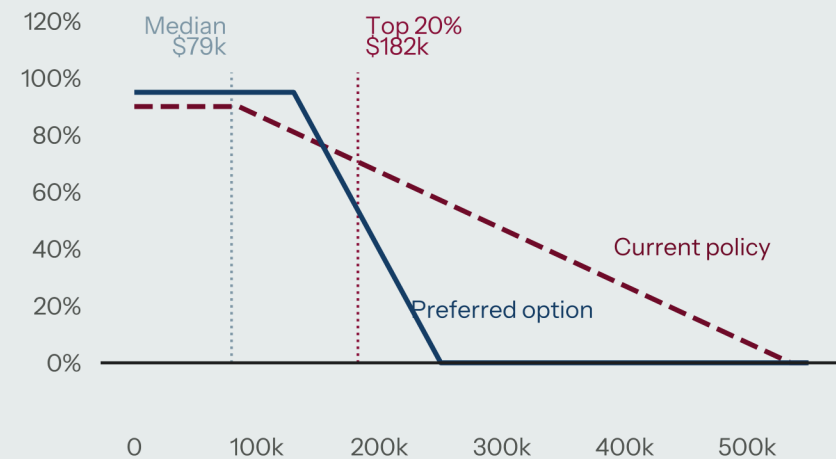
<sup>56</sup> Department of Education (2025).

<sup>57</sup> Using HILDA, we estimate that fewer than 5% of families receiving the Child Care Subsidy have more than two kids in pre-school child care. Disincentives to work are discussed in Appendix A.

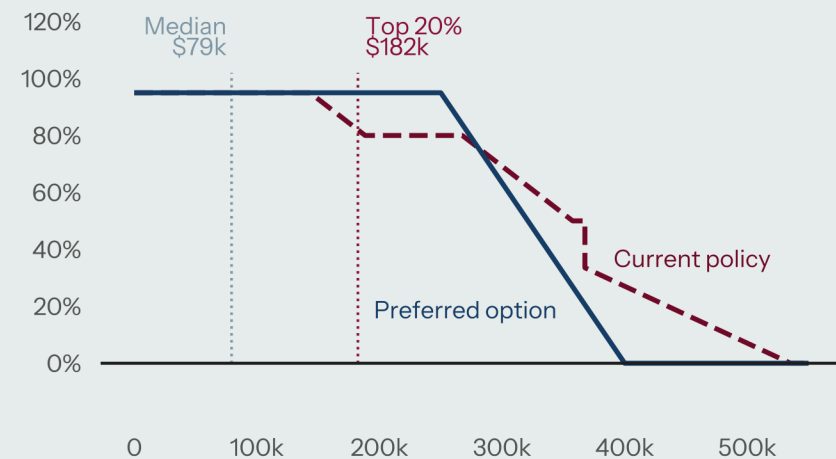
FIGURE 11

### Child Care Subsidy test: current vs preferred option

*First Child:* Child Care Subsidy rates against pre-tax household income



*Second and Younger Children:* Subsidy rates against pre-tax household income



Note: Under current policy, second and younger children use the higher-rate schedule only while family income is less than \$367,563. At \$367,563 and above, they fall back to the first-child standard rate.

Source: Policy Institute Australia Microsimulation Model (PIAMM).

#### 4.2.2 The preferred option generates savings and improves equity

As shown in Figure 12, our preferred option modestly increases average support for recipient households across the income distribution, except for the top 20%. This result is driven by the higher first child subsidy rate (95% v 90%) and higher threshold for the full subsidy (\$133,000 v \$85,279).

Smaller average subsidies are being paid to households in the top 20% of the income distribution, with annual income above \$182,000.

The reform meaningfully improves the targeting of the Child Care Subsidy. Under current settings, a *lower* average benefit of \$10,800 is paid to families in the bottom 20% of the income distribution, while the average benefit to the top 20% is \$13,600 — a ratio of 0.8 (Figure 12). Average benefits are regressive in part because high income families are more likely to use more approved child care. Under our preferred option, this switches, with the ratio increasing to 1.7 — that is, recipient households in the bottom 20% of the income distribution receive 1.7 times the benefit of recipient households in the top 20%.

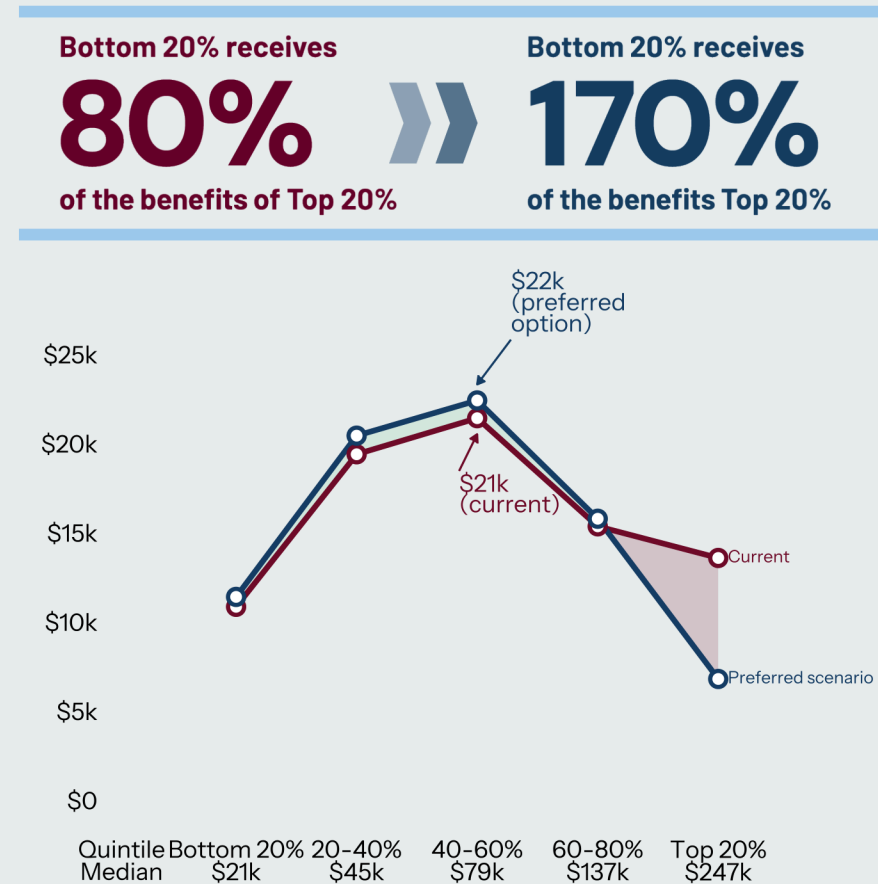
Child care is expensive. 'Approved' child care costs about \$150 per day, or \$39,000 per year for one child in care five days a week. With no subsidy, the family must meet this cost themselves — a significant expense even for a high income family. But if the family was eligible for a 95% subsidy, the benefit would be worth \$36,136 per year. While examining how the Child Care Subsidy affects prices is beyond the report's scope, the ACCC has found that 'when subsidies increase, out-of-pocket expenses decline initially but then tend to revert to higher levels ... because subsequent fee increases erode some of the intended benefit for households over time'.<sup>58</sup>

<sup>58</sup> Australian Competition & Consumer Commission (2023).

FIGURE 12

#### Modelled outcome: Better targeting shifts the Child Care Subsidy away from high income families

Average annual Child Care Subsidy per current recipient household, by income



Source: Policy Institute Australia Microsimulation Model (PIAMM).

Our preferred option would reduce expenditure on the Child Care Subsidy by about \$3.2 billion a year. Almost all of that comes from high-income families in the top 20% of the income distribution.

Figure 13 shows how families across the income distribution are affected by the preferred option to change the Child Care Subsidy.

For high-income families in the top 20% of the income distribution, around 500,000 families — half of all current recipients — would see a reduction in the benefit they receive.<sup>59</sup> This reflects the current concentration of Child Care Subsidy recipient families towards the top of the income distribution, as high-income families are more likely to access formal child care. For example, a household with combined income of \$250,000 and two kids in child care 5 days a week might see a decrease in their annual subsidy from \$52,100 to \$36,100.

More than 180,000 lower- and middle-income families in the bottom 60% of the income distribution, or about one fifth of current recipients, would see a modest increase in the total subsidy they receive. The scatterplot in Figure 13 shows how this would affect households across the distribution, with an average increase of around \$500 to \$1,000 for lower income and middle income families. For families who are high users of child care, this could be even higher. For example, a household with combined income of \$120,000 and two kids in child care 5 days a week might see an increase in their annual subsidy from \$67,700 to \$72,300. These are the families for whom affordability is most likely to shape parents' decisions about work (Section 4.2.3).

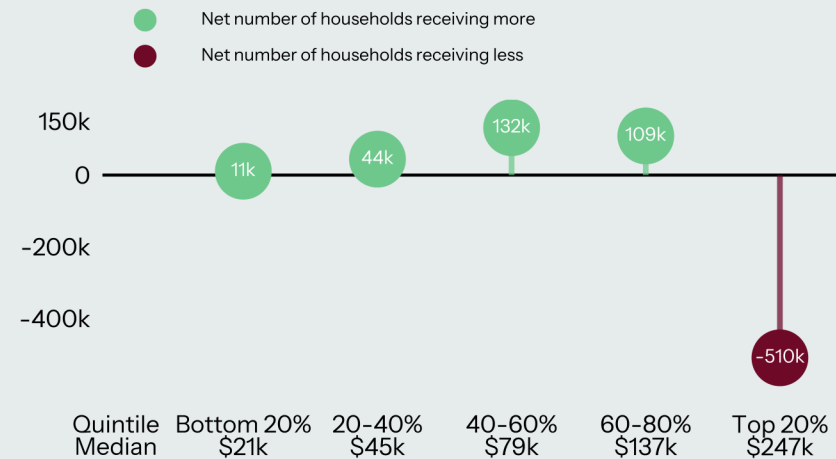
The reform reduces the cost of formal care and supports workforce participation, while pulling back support for households with the greatest means.

<sup>59</sup> Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

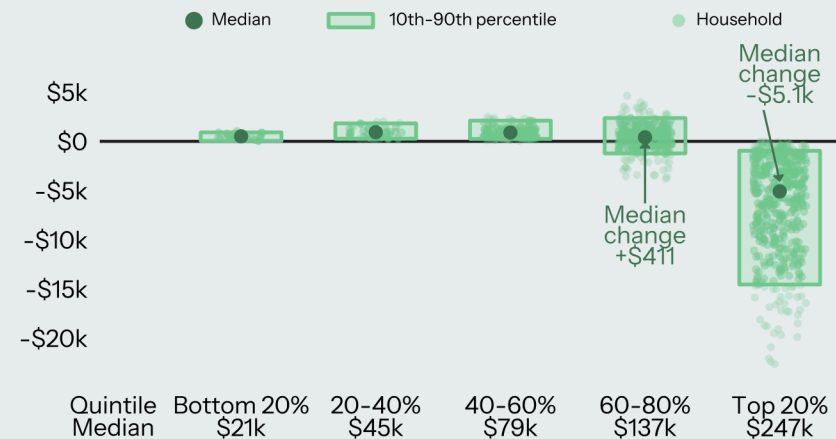
FIGURE 13

**Modelled outcome: Reductions concentrated in the top 20%**

*Net number of current recipient households receiving more/less Child Care Subsidy, by income*



*Distribution of Child Care Subsidy payment changes among current recipient households, by income*



Source: Policy Institute Australia Microsimulation Model (PIAMM).

### 4.2.3 How would this change affect incentives to work?

A key aim of the Child Care Subsidy is to encourage workforce participation by reducing the cost of child care, thereby increasing the financial incentive for paid work.

When the Commonwealth Government introduced the Child Care Subsidy in 2018,<sup>60</sup> they indicated it would draw 230,000 families into more paid work.<sup>61</sup> However, the impact was much more limited, with about one tenth that number reporting more work — and an overall 1.4% increase in hours worked for single parents, and 0.3% for coupled parents.<sup>62</sup>

In 2004, the introduction of the Child Care Tax Rebate had a similarly limited effect — boosting mothers' hours of work by just one hour on average.<sup>63</sup>

Even these limited gains may *not* be the result of child care subsidies, since in both cases the employment uptick roughly aligned with pre-existing trends.<sup>64</sup>

In general, Australian studies suggest the labour supply response to child care prices is modest. A 1% reduction in child care cost is associated with an increase in maternal participation of roughly 0.02–0.29% and hours worked of 0.02–0.65%. Most estimates sit below 0.2%, broadly consistent with international evidence.<sup>65</sup> This means that to increase maternal hours worked by 2%, child care costs would need to decline by *more than 10%*.

Responsiveness is higher among lower-wage and lower-income mothers, single

<sup>60</sup> Replacing the Child Care Tax Rebate and the Child Care Benefit.

<sup>61</sup> Porter (2016).

<sup>62</sup> Bray et al. (2021).

<sup>63</sup> Productivity Commission (2024b).

<sup>64</sup> Bray et al. (2021).

<sup>65</sup> Productivity Commission (2024b).

parents, mothers with preschool-aged children, and secondary earners; it is lower for higher-income families, fathers, married men, and households whose work decisions are shaped more by preferences, job flexibility, or service availability.<sup>66</sup>

#### Workforce disincentive rates

Workforce disincentive rates reflect how much pre-tax income is retained. This is the result of tax rates, but also the phase out of other social transfer payments. For example, depending on the income of their partner, someone earning \$50,000 in pre-tax income may face a tax rate of 32% and a 30% phase out of Family Tax Benefit A, meaning a workforce disincentive rate of 62%.<sup>67</sup> This means that for every \$100 of additional pre-tax income that is earned, only an additional \$38 is pocketed by the worker.

Evidence indicates that workers' responses to changes in workforce disincentive rates are real but modest on average, with the decision of whether or not to work at all more responsive to workforce disincentive rates than decisions around how many hours to work. Primary earners are relatively unresponsive; secondary earners, single parents, and those on lower incomes are much more likely to adjust their hours. Where workforce disincentive rates are very high they can strongly discourage extra work, particularly for sole parents and secondary earners.<sup>68</sup>

Overall workforce disincentive rates reflect the broader tax-transfer system, and for most households, child care costs are not the primary driver.<sup>69</sup> However,

<sup>66</sup> Department of the Treasury (2024); Dandie and Mercante (2007).

<sup>67</sup> Including 2% the Medicare levy.

<sup>68</sup> Productivity Commission (2024a); Department of the Treasury (2024); Dandie and Mercante (2007).

<sup>69</sup> Productivity Commission (2024a).

the effect of child care can be material, and for some households may affect workforce decisions.

Child care subsidies affect parents' work decisions through two main channels. First, they reduce the price families pay for child care, making work more financially attractive.<sup>70</sup> Second, as subsidies phase out with income, workers keep less of each extra dollar earned, weakening the incentive to work more. The relative magnitude of these effects on work decisions is actively debated, and varies by income, education, and sex.<sup>71</sup>

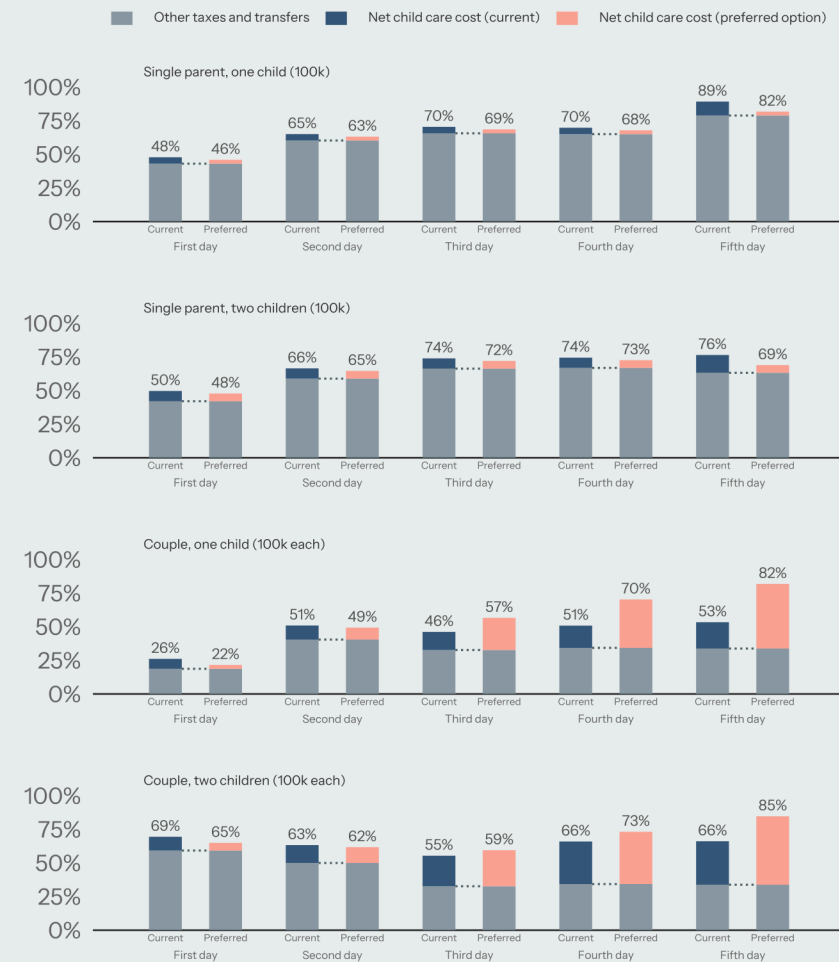
We combine these together to calculate the 'net child care' effect on workforce disincentive rates. For example, a single parent with capacity to earn \$150,000 a year full time is currently working four days a week and has their only child in paid care for that many days. If they choose to work a fifth day each week, then under our preferred option the additional amount they pay for child care for that day each week is about \$34 (\$150 total cost minus a subsidy of 77%). But because their subsidy rate falls from 95% to 79%, they must also pay an additional \$93 each week in relation to the other four days their child is in care. So their net child care cost is \$127, or 22% of the additional money they expect to earn, which is added to their workforce disincentive rate.<sup>72</sup>

Figure 14 shows how workforce disincentive rates vary for parents under current settings and under our preferred option for the Child Care Subsidy.

FIGURE 14

### A better targeted Child Care Subsidy reduces workforce disincentives for some households

*Workforce disincentive rate\* shown includes average child care cost net subsidy, plus taxes and the phase out of other transfers. A higher WDR reduces incentive to work.*



\* A workforce disincentive rate measures the share of pre-tax income lost to tax and the phase-out of social transfers, reducing the financial return from earning more. Source: Policy Institute Australia modelling.

<sup>70</sup> Noting subsidies may increase system costs over time.

<sup>71</sup> Productivity Commission (2024b); Department of the Treasury (2024); Dandie and Mercante (2007).

<sup>72</sup> Our approach follows Wood et al. (2020).

Each panel shows a different representative family (single/dual parent; 1 or 2 kids in child care) and maps how disincentive rates change: for the 'first day' in the week they work (and put their child in care), the 'second day', and so on.<sup>73</sup> In dual parent families, we assume one parent works full time, and the decision about how much to work is just for the second parent. Figure 14 assumes that all parents earn the median full-time employee earnings of \$100,000 per year.

We assume that the number of days worked by the single or second parent is equal to the number of days their kids are in formal child care. In reality, many families have alternative arrangements — such as those who opt to put children in child care for more days than they work, or where care is provided at no cost by a relative — so that working an extra day would not require an extra day of paid child care. Of 1 to 4-year-olds receiving care outside the home, around half received some informal care, most often from a grandparent.<sup>74</sup>

The grey bars in Figure 14 represent the workforce disincentive rates for other taxes and transfers (that is, *not* including child care). These do not vary between the preferred option and current settings, as shown by the dotted lines. The pink and blue bars show the 'net child care' effect on workforce disincentive rates. For example for a single parent family with one child and earning capacity of \$100,000 per year looking at working a fifth day (shown in the top panel), the workforce disincentive of other taxes/transfers is about 80%, the net child care effect raises this to 89% under current settings. Under our preferred option it is lower at 82%. This means that the parent would pocket \$18 instead of \$11 out of every \$100 of pre-tax income earned.

<sup>73</sup> We estimate that just 4.5% of families who access the Child Care Subsidy have more than 2 children in formal child care at a time.

<sup>74</sup> Australian Institute of Health and Welfare (2019).

This example fits with the Productivity Commission's finding in its 2024 Child Care report that child care is *not* the primary driver of high workforce disincentive rates for lower income earners. Rather, the PC suggested the disincentive sits in income tax settings combined with the steep phase out of other social supports as incomes rise. Child care subsidies should be designed with this in mind.<sup>75</sup>

Our 'preferred option' has been designed to better target the Child Care Subsidy at those who need it, *reduce* the disincentive to work for lower income earners, and minimise the disincentive for higher income earners.

As shown in Figure 14, our preferred option modestly *reduces* the workforce disincentive rate for the single parent families, and for the second parent in dual parent families to work the first or second day per week (that is, whether to work part time versus not working at all). However, it *increases* the workforce disincentive rates for them to work days beyond that (Figure 14). Disincentives to work for a range of other representative family types are shown in Appendix A.

In general, our preferred option will *reduce* workforce disincentive rates for lower- and middle-income households, but *increase* workforce disincentive rates for higher-income households. These results are driven by the higher maximum first child subsidy rate of 95%, the higher full subsidy threshold, and the faster phase out beyond this threshold.

The decision of whether and how much to work is rarely just a financial decision. Work decisions are also shaped by non-financial factors — child care availability, job flexibility, career considerations, and other personal preferences.<sup>76</sup>

<sup>75</sup> Productivity Commission (2024a).

<sup>76</sup> Productivity Commission (2024b).

#### 4.2.4 How would this change affect outcomes for children?

Some proponents of the Child Care Subsidy argue that its primary benefit sits in the benefits that formal, approved child care can bring for children's early learning and development.<sup>77</sup>

There is limited evidence from Australia on whether formal child care improves outcomes for children, but evidence from other countries consistently shows significant benefits *for children experiencing disadvantage*. The benefits for children of higher income families are less clear.<sup>78</sup> In Norway, expanded ECEC increased earnings for children (in adulthood) in the bottom two-thirds of the income distribution – with a much larger effect for the bottom third – but showed no significant effect for children in the top third.<sup>79</sup> In Finland, child care led to significant benefits at the 10th income percentile, but not at the median, and led to *adverse* effects on children at the 90th income percentile.<sup>80</sup>

Of course, child care subsidies can only improve developmental outcomes for children where they increase participation in quality early child care. In line with our findings in relation to labour force participation in Section 4.2.3, evidence suggests the effect of the subsidy on child care demand is modest, especially at high incomes.<sup>81</sup>

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<sup>77</sup> Productivity Commission (2024b).

<sup>78</sup> Productivity Commission (2024b).

<sup>79</sup> Havnes and Mogstad (2015).

<sup>80</sup> Silliman and Mäkinen (2022).

<sup>81</sup> Productivity Commission (2024b).

## Alternative options

Our preferred option aims to better target the Child Care Subsidy on families who have less capacity to pay for child care themselves, focusing on means as indicated by income. We have modelled two alternative options, the results for which are presented in Table 3.

The **\$1.5m Asset Test** option matches our preferred option, but also adds an asset test so that any family with less than \$1.5 million in net assets<sup>82</sup> receives what they would receive under our preferred option, but any family above this assets threshold receives no subsidy. About 10% of all Child Care Subsidy recipient households fail this asset test — putting them in the top 30% of the wealth distribution (and with an average age of just 41 for the adults). The results indicate that even with a much stricter income test, there are many families that are eligible for significant subsidies whose wealth suggests they have capacity to pay for child care themselves.

The **Universal** option reflects public statements by Prime Minister Albanese about his desire for a universal child care system.<sup>83</sup> We follow the Productivity Commission in modelling this as a flat 90% subsidy for all households.<sup>84</sup> The cost is \$5.5 billion a year more (over 30% more than the current system), with \$7,700 more going to recipient households in the top 20%, and less going to lower- and middle-income households. In its 2024 report, the PC concluded that a universal 90% subsidy comes at a higher cost and does not prioritise families experiencing disadvantage.<sup>85</sup>

<sup>82</sup> Including owner-occupied housing but not including superannuation.

<sup>83</sup> Albanese et al. (2024).

<sup>84</sup> Productivity Commission (2024b).

<sup>85</sup> The PC also modelled a \$10 a day flat fee Productivity Commission (2024b).

TABLE 3

Child Care Subsidy: alternative options compared

FEATURE	UNIVERSAL: 90% SUBSIDY	PREFERRED OPTION	PREFERRED + ASSETS >\$1.5M
<b>2025–26 fiscal impact</b>	\$5.5 billion cost	<b>\$3.2 billion saving</b>	\$3.7 billion saving
<b>2025–26 program spend</b>	\$211 billion	<b>\$12.4 billion</b>	\$11.9 billion
<b>Change in average household payment: top 20% of income distribution</b>	+\$7,710	<b>-\$6,784</b>	-\$7,201
<b>Change in average household payment: bottom 20% of income distribution</b>	-\$45	<b>+\$556</b>	+\$556
<b>Ratio: bottom 20% to top 20% average payment by income</b>	0.5 (curr. 0.8)	<b>1.7</b> (curr. 0.8)	1.8 (curr. 0.8)

Note: Fiscal impact and payment changes are measured against current settings. Spend under current settings is \$16.4 billion. The asset test excludes superannuation and counts full home equity.

Source: Policy Institute Australia Microsimulation Model (PIAMM).

## 4.3 Better targeting Parental Leave Pay

### 4.3.1 A stricter income test

Parental Leave Pay is available to parents of newborns and recently adopted children who were in regular paid work prior to the birth or adoption. It is paid to around 180,000 families each year.<sup>86</sup> In 2025–26, Parental Leave Pay is paid for up to 120 days (or 24 weeks based on a five-day work week) at the national minimum wage (\$948 per week pre-tax), meaning that in total it is worth up to \$22,754 per child. Eligible single parents can claim the full 120 days. For dual-parent families, the 120 days can be shared between them, although at least 15 days is reserved for the second parent.<sup>87</sup>

As outlined in Section 3.2, families with very high incomes can receive substantial Parental Leave Pay benefits.

Our 'preferred option' aims to better target Parental Leave Pay at lower- and middle-income households that have less financial capacity to absorb the income foregone during the leave period.

- It lowers the household income threshold for the full Parental Leave Pay entitlement from \$373,000 to \$200,000.
- It removes the separate individual income threshold (currently set at \$180,000) so that households with incomes above the household income threshold cannot claim a substantial benefit.

Our preferred option is detailed in Table 4.

<sup>86</sup> Plibersek et al. (2025).

<sup>87</sup> For babies born from 1 July 2026, the benefit is legislated to increase to 130 days (equivalent to \$24,650 using 2025–26 rates), with at least 20 days reserved for the second parent.

TABLE 4

Parental Leave Pay: current vs preferred option

FEATURE	CURRENT SCHEME	PREFERRED OPTION
<b>Family income limit (full entitlement)</b>	Full Parental Leave Pay available for families with combined income up to <b>\$373,000</b> .	Full Parental Leave Pay available for families with combined income up to <b>\$200,000</b> .
<b>Individual income limit (partial entitlement)</b>	Up to <b>21 of 24 weeks</b> available to families with higher combined income, if one partner has individual income below <b>\$180,000</b> .	No partial entitlement for families with combined income above <b>\$200,000</b> .
<b>Taper rate</b>	No taper	No taper, to align with the current system.

Source: Policy Institute Australia analysis.

### 4.3.2 How would this change affect outcomes across the distribution?

Our preferred option would reduce the parental leave payments to some households in top 20% of the income distribution – those with household income above \$200,000. There is no effect on households across the rest of the income distribution.

In 2025–26, the Commonwealth will spend about \$4.7 billion on Parental Leave Pay.<sup>88</sup> Under our preferred option, this would fall to about \$3.2 billion, with about \$1.5 billion less going to households with incomes above \$200,000.

Just over 90,000 households would see a reduced benefit (Figure 15).

They typically lose either the full amount of \$22,754, or if only one parent is currently eligible, \$19,910 (Figure 15).

As noted above, many of these parents would be eligible for employer-funded paid parental leave, typically at their prevailing wage. More than 70% of workers that are in the top 50% of income earners have access to employer-funded paid parental leave.<sup>89</sup> Linking access to government-funded Parental Leave Pay to whether a household has access to employer-funded paid parental leave could help target the benefit at those who need it, but is beyond the scope of this analysis.

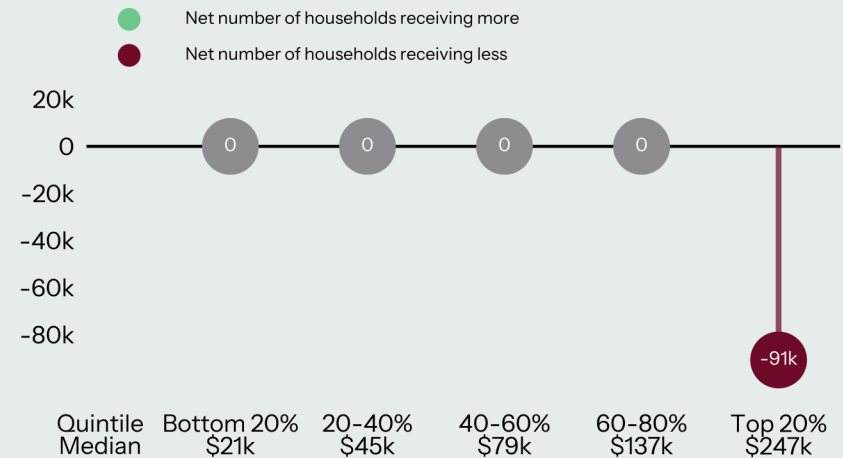
<sup>88</sup> Department of Social Services (2026b).

<sup>89</sup> Australian Bureau of Statistics (2025b).

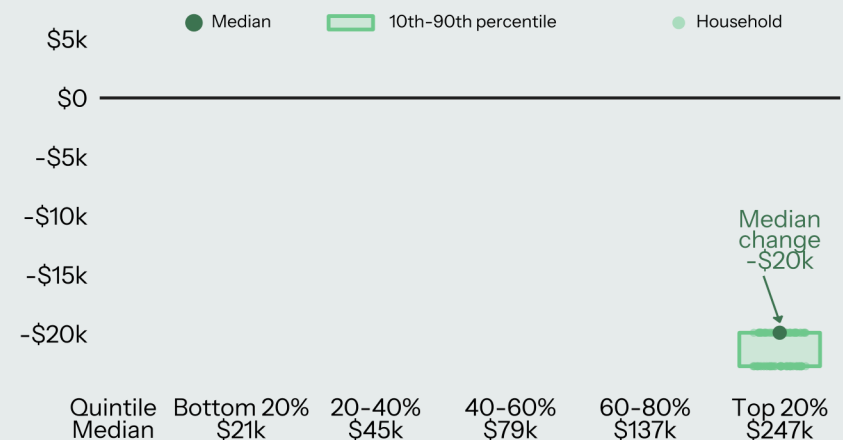
FIGURE 15

### Reform would reduce benefits for households in the top 20% of the income distribution

Net number of current recipient households receiving more/less Parental Leave Pay, by income quintile



Distribution of Parental Leave Pay payment changes among current recipient households, by income quintile



Source: Policy Institute Australia Microsimulation Model (PIAMM).

### 4.3.3 How would this change affect leave taking and workforce participation by parents?

The *Paid Parental Leave Act 2010* (Cth) outlines its objectives: to signal that taking time out of the paid workforce to care for a child is part of the usual course of life and work for both parents; promote equality between men and women and balance between work and family life; and provide financial support to parents caring for children, including to encourage women to continue to participate in the workforce, and to increase time off by fathers and partners. This section examines the evidence on labour market outcomes.

The most relevant evidence on the effects of Australia's Parental Leave Pay scheme comes from older evaluations comparing outcomes for families welcoming children just prior to and just after the policy was introduced in 2011, particularly the comprehensive evaluation of Martin et al (2014).<sup>90</sup> It found evidence that the scheme delayed working mothers' return to work up to about the time their babies reach six months of age, and also that it increased the likelihood that mothers would return to work by the time their babies were 12 months old.

However, the evaluation also found that both the leave taking and return to work effects were much larger for women with low incomes than for women with high incomes — defined as those in the top third of the income distribution, with pre-birth pre-tax income higher than around \$85,000 in \$2025–26, and excluding women with incomes above \$150,000 (around \$215,000 in \$2025–26 who were ineligible).<sup>91</sup> For the high income group, mothers with access to the

<sup>90</sup> Martin et al. (2014). The scheme has been reformed since the evaluation was undertaken, although its structure is broadly the same.

<sup>91</sup> Martin et al. (2014).

scheme were 2% more likely to have returned to work at 52 weeks, although this result was not statistically significant. A later study found that the effect was larger for women without access to employer-funded paid parental leave.<sup>92</sup>

The evaluation found that the scheme has minimal effect on the work decisions of fathers — making it more likely that they took leave close to the baby's birth, but not affecting the total amount of leave that they took in the first 6 months of the baby's life.<sup>93</sup>

The authors of the evaluation concluded:<sup>94</sup>

The evaluation has shown that much of the important impact of Paid Parental Leave occurs because of the financial security this income provides families, and the additional time it allows some mothers to remain at home with their newborns. These effects do vary depending on family circumstances. In some families, the security of income provided by Paid Parental Leave is especially important, while in others family income security is already assured.

International evidence supports the finding that government-provided paid maternity leave encourages leave taking and longer term workforce attachment by mothers (although leave of greater than a year can have negative effects).<sup>95</sup>

However, in most wealthy countries, the benefit is linked to a mother's earnings prior to the birth, and Australia is unusual in providing a flat benefit at the minimum wage.<sup>96</sup> As a result, there are few international studies on the extent to

<sup>92</sup> Broadway et al. (2020).

<sup>93</sup> The original scheme set aside 2 weeks as Dad and Partner Pay. Martin et al. (2014).

<sup>94</sup> The scheme was originally known as Paid Parental Leave, which included Parental Leave Pay and Dad and Partner Pay. Martin et al. (2014).

<sup>95</sup> Rossin-Slater (2017); Anand et al. (2026).

<sup>96</sup> Rossin-Slater (2017).

which these findings hold for women or families across the income distribution, but those that look at this issue find that the effect of paid leave is much higher for low income parents.<sup>97</sup>

Overall, there is very strong evidence that Parental Leave Pay supports leave-taking and labour force attachment, particularly for lower-income mothers. What is less clear from the available evidence is the extent to which these results hold for the highest-income households — those targeted by our preferred option — and especially where these families also have access to employer-funded paid parental leave. The available evidence, and the relative financial value of a flat minimum-wage payment to these households, suggest that for families with combined income above \$200,000, the government-funded benefit is far less likely to be a decisive factor in parents' decisions about leave-taking or return to work.

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<sup>97</sup> Joseph et al. (2013); Rossin-Slater et al., 2013.

## Alternative options

Our preferred option aims to better target Parental Leave Pay to families who have less capacity to fund parental leave themselves, focusing on means as indicated by income.

We have modelled two alternative options, results for which are presented in Table 5.

The **Current + Assets > \$1.5m** option matches *current* settings, but adds a \$1.5 million asset test threshold.<sup>98</sup> Any family with wealth below this threshold receives what they would receive under current settings, but any family with wealth above this threshold receives no Parental Leave Pay. About 5% of current Parental Leave Pay recipient households fail this asset test – putting them in the top third of the wealth distribution, even without counting their super (and with the adults in these households having an average age of 39).

The **Preferred + Assets > \$1.5m** option matches our preferred option, but also adds an asset test so that any family with less than \$1.5 million in net assets<sup>99</sup> receives what they would receive under our preferred option, but any family with wealth above this assets threshold receives no Parental Leave Pay.

TABLE 5

### Parental Leave Pay: alternative options compared

FEATURE	PREFERRED OPTION	CURRENT + ASSETS > \$1.5M	PREFERRED + ASSETS > \$1.5M
<b>2025–26 fiscal impact</b>	<b>\$1.5 billion saving</b>	\$153 million saving	\$1.6 billion saving
<b>2025–26 program spend</b>	<b>\$3.2 billion</b>	\$4.55 billion	\$3.1 billion
<b>Change in average household payment: top 20% of income distribution</b>	<b>-\$15,620</b>	-\$706	-\$15,717
<b>Ratio: top 20% to bottom 40% average household payment by income</b>	<b>0.3</b> (curr. 1.0)	1.0 (curr. 1.0)	0.3 (curr. 1.0)

Note: Fiscal impact and payment changes are measured against current settings. Spend under current settings is \$4.7 billion. Average payment changes use baseline Parental Leave Pay recipients by HILDA-wide income quintile. The asset test excludes superannuation and counts full home equity.

Source: Policy Institute Australia Microsimulation Model (PIAMM).

<sup>98</sup> Including owner-occupied housing but not including superannuation.

<sup>99</sup> Including owner-occupied housing but not including superannuation.

## 4.4 Better targeting the Age Pension

### 4.4.1 How to better target the Age Pension

In 2024–25, 2.7 million Australians aged 67 years and older (or 60% of retirees) received a full or part Age Pension.<sup>100</sup> The full Age Pension is paid at a rate of \$31,200 per year for singles and \$47,100 per year for couples (combined).<sup>101</sup>

As discussed, a pensioner’s owner-occupied home is effectively counted in the assets test thresholds for means testing the pension. However, all homeowners have the value of their home treated the same — with an effective value of \$258,000 — regardless of whether their home is worth \$500,000 or \$5 million. Owners of both modest and lavish homes are treated more favourably than a non-homeowner (Section 3.3).

Our preferred option to better target the Age Pension (Table 6) aims to address this inequity.

- It provides more equitable treatment of households with substantial equity in owner-occupied housing, by including the net value of owner-occupied housing above \$500,000 in the assets test.<sup>102</sup>
- It lifts the asset test threshold for homeowners by \$258,000 to match non-homeowners, removing the mechanism by which every retiree’s home is accounted for in the current asset test

<sup>100</sup> Australian Institute of Health and Welfare (2025a).

<sup>101</sup> The rate is indexed twice yearly to the highest out of wages and prices. In addition to the base rate, pensioners may receive supplementary payments including Pension Supplement, Energy Supplement, and Rent Assistance (for non-homeowners). Services Australia (2026c).

<sup>102</sup> Automated Valuation Models, which value properties based on large datasets, are already used in mortgage valuation processes in Australia, and could be used for valuing properties for assets tests (Derwin, 2026).

TABLE 6

### Age Pension asset test: current vs preferred option

FEATURE	CURRENT ASSETS TEST	PREFERRED OPTION
<b>Owner-occupied home</b>	All owner-occupied housing is accounted for but effectively valued at <b>\$258,000</b>	The first <b>\$500,000</b> (indexed to inflation) of owner-occupied housing equity is excluded. Housing equity above this amount is included
<b>Single full-pension threshold</b>	Homeowners is <b>\$321,500</b> , while non-homeowners is <b>\$579,500</b> .	<b>\$579,500</b> for all, regardless of homeownership status (with the first <b>\$500,000</b> of home equity excluded).
<b>Single part-pension cut-off</b>	Homeowners is <b>\$714,500</b> , while non-homeowners is <b>\$972,500</b> .	<b>\$972,500</b> for all, regardless of homeownership status (with the first <b>\$500,000</b> of home equity excluded).
<b>Couple full-pension threshold</b>	Homeowners is <b>\$481,500</b> , while non-homeowners is <b>\$739,500</b> .	<b>\$739,500</b> for all, regardless of homeownership status (with the first <b>\$500,000</b> of home equity excluded).
<b>Couple part-pension cut-off</b>	Homeowners is <b>\$1,074,000</b> , while non-homeowners is <b>\$1,332,000</b> .	<b>\$1,332,000</b> for all, regardless of homeownership status (with the first <b>\$500,000</b> of home equity excluded).

Source: Policy Institute Australia analysis.

#### 4.4.2 How would this change affect who receives the pension?

Under our proposed changes, pensioners residing in modest homes with modest means will find it easier to meet the assets test, with some receiving higher pension payments. Pensioners residing in high value homes will see that asset treated more like other forms of wealth. Around 80% of full pensioners would continue to receive the full pension, and around 75% of part pensioners will continue to receive a part pension. Non-homeowners would experience no change.

The changes would save around \$10 billion a year, with most of the savings coming from households in the top 20% of the wealth distribution.

The main beneficiaries of our alternative approach are retirees with homes of modest value, who are around the middle of the wealth distribution. Homes valued at less than \$500,000 will not count toward the asset base. Households in this group (accounting for about 420,000 people, or about one in six pensioners) will be able to hold an additional \$258,000 in assets compared to the current assets test and still receive the full pension, or receive a larger part pension.

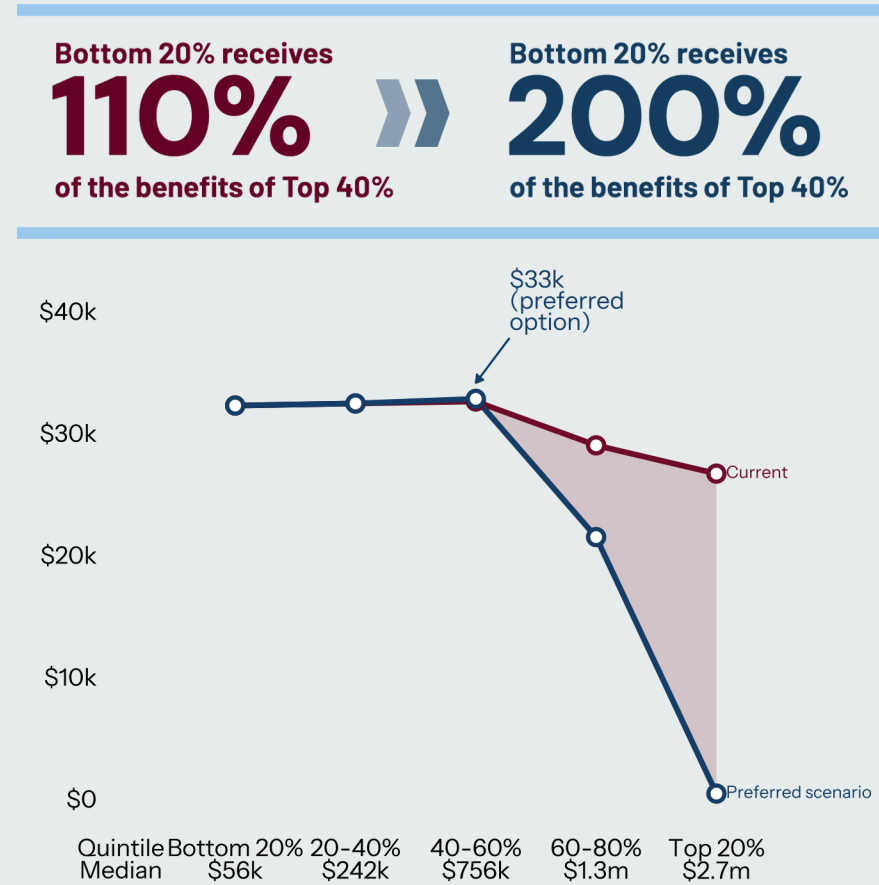
A single retiree living in a home valued at a bit over a million dollars, or a retiree couple in a home valued at up to around \$1.2 million, would still be eligible to receive the full pension if they didn't have substantial other assets. These values are higher than the Australia-wide median dwelling value of \$930,000 and capital city median dwelling value of \$1.0 million.<sup>103</sup>

<sup>103</sup> Cotality (2026).

FIGURE 16

#### Reform would see the Age Pension shift away from top 20% by wealth

Average annual Age Pension payment per current recipient household, by wealth



Source: Policy Institute Australia Microsimulation Model (PIAMM).

Retiree homeowner households with total assets above \$1.47 million for singles, or \$1.83 million for couples, including the total net equity of their owner-occupied housing, would no longer be eligible for a pension. Those with assets above \$1.08 million for singles, or \$1.24 million for couples, would remain eligible for a part pension, but not a full pension.<sup>104</sup>

Figure 16 shows that, for Age Pension recipients in the top 20% of the wealth distribution (with wealth above \$1.8 million), the average pension reduction would be about \$26,000 a year. Outcomes would vary between households, depending for example on their housing equity and other assets.

Figure 17 shows the impact on the roughly 450,000 retiree households that would receive reduced benefits.<sup>105</sup> This represents about 17% of retiree households, all sitting in the wealthiest 40% of Australian households.

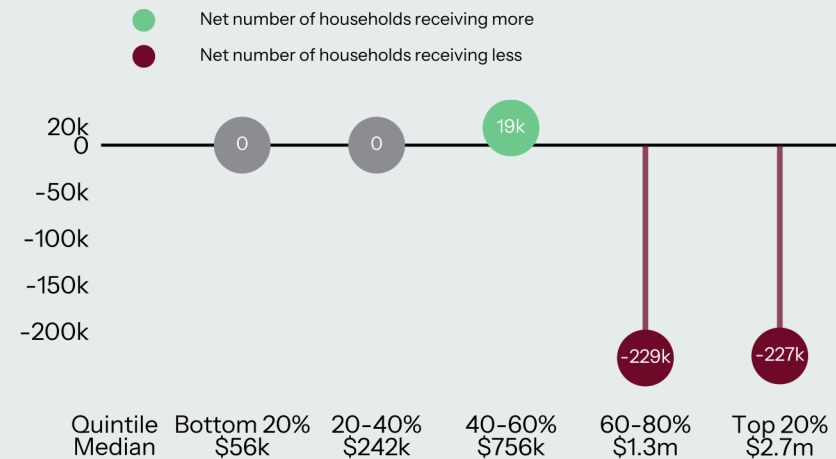
For Age Pension recipients in the 60–80% wealth quintile, with wealth roughly between \$1.0 million and \$1.8 million, the average annual Age Pension receipt falls from around \$28,990 to around \$21,467. This is an average reduction of about \$7,500 a year, much smaller than the reduction for the top wealth quintile.

While this group all have substantial means, some may benefit from assistance in accessing the equity in their assets to meet their living expenses. Section 5.2 proposes a new policy solution with this aim.

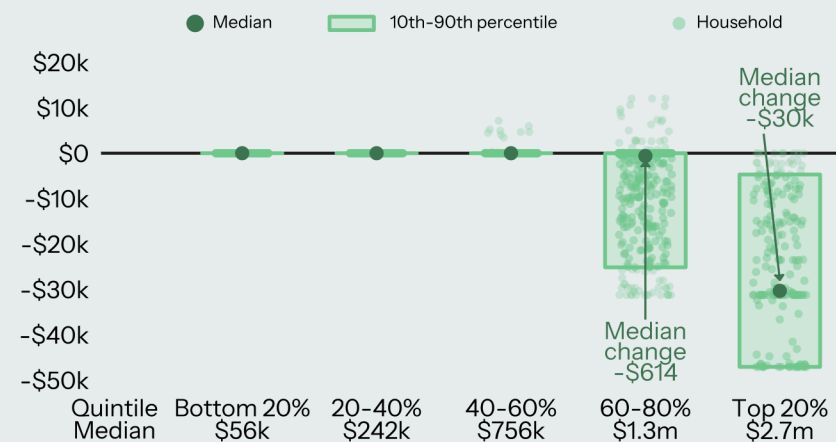
FIGURE 17

**About 17% of retiree households (all with wealth above about \$1.1m) would receive less**

*Net number of current recipient households receiving more/less Age Pension, by wealth quintile*



*Distribution of Age Pension payment changes among current recipient households, by wealth*



<sup>104</sup> These cutoffs assume net owner-occupied housing wealth above \$500,000.

<sup>105</sup> Note that this is a net change.

Source: Policy Institute Australia Microsimulation Model (PIAMM).

## Alternative options

Our preferred option aims to strike a balance between addressing the horizontal and vertical inequities identified above (Section 3.3), while accounting for the particular characteristics of owner-occupied housing and the role of owner-occupied housing for older Australians.

We have modelled two alternative options, results for which are presented in Table 7.

The **Full Home Equity option** has the same increase to assets test thresholds for homeowners, but includes the full equity value of owner-occupied housing in the asset test. This option fully addresses the horizontal inequity between homeowners and non-homeowners, and the vertical inequity that follows from treatment of households with different value homes. It leads to a large reduction in pension payments for many households — with about twice as many households receiving less than under our preferred option, and savings in 2025–26 of more than \$23 billion. The savings are much less well targeted at the top 20% of the wealth distribution, compared to our preferred option.

The **Home Equity > \$1 million option** has the same increase to assets test thresholds for homeowners, but only the equity value of owner-occupied housing above \$1,000,000 is included in the assets test.<sup>106</sup> This option does less to address horizontal and vertical inequities, but with all of the savings coming from the top 20% of the wealth distribution. One option would be to set a higher threshold such as \$1 million but to fix it in nominal terms so a greater proportion of owner-occupied housing value is counted over time as house prices rise.

<sup>106</sup> Broadly equivalent to the Australia-wide median home price of \$930,000.

TABLE 7

### Age Pension asset test: alternative options compared

	FULL HOME EQUITY	PREFERRED: EQUITY >\$500K	EQUITY >\$1M
<b>Annual fiscal saving</b>	\$23.5 billion	<b>\$9.9 billion</b>	\$4.1 billion
<b>Full pensioners retaining full pension</b>	53%	<b>81%</b>	92%
<b>Share of savings from top 20% by wealth</b>	27%	<b>62%</b>	100%
<b>Ratio: bottom 20% to top 20% average pension</b>	306.8 (curr. 1.6)	<b>75.5</b> (curr. 1.6)	5.0 (curr. 1.6)
<b>Share of pensioners receiving less</b>	53%	<b>25%</b>	11%
<b>Home value where pension may reduce (single)</b>	Any home value	Above <b>~\$1.1m</b>	Above <b>~\$1.6m</b>
<b>Median capital city couple*</b>	Reduced — home equity fully counted	Still eligible for <b>full pension</b>	Still eligible for full pension

\* Couple aged 67 owning a median capital city dwelling (~\$1,030,000) with \$200,000 in other assets.

Note: All options assume assets test thresholds for homeowners raised ~\$258,000 to match non-homeowners.

Source: Policy Institute Australia Microsimulation Model (PIAMM).

## 4.5 Better targeting Aged Care support

### 4.5.1 Greater inclusion of owner-occupied housing

Like the Age Pension, owner-occupied housing is a significant matter in Aged Care (which includes both Residential Aged Care and Support at Home). The current system either excludes it completely or caps its value at just \$214,884 in the Aged Care assets tests. This means that, in practice, almost all homeowners have the value of their home treated the same (as few homes are valued lower than the cap), while homeowners are treated more favourably than non-homeowners. Caps on private contributions compound this inequity.

Our preferred option to better target Aged Care aims to address this inequity.

- It provides more equitable treatment between homeowners and non-homeowners by removing exemptions that exclude owner-occupied housing wealth from assets tests when the house is occupied by the recipient or a 'protected person' such as their partner.
- It provides more equitable treatment of homeowners with substantial equity in owner-occupied housing, by including its value above \$500,000 in assets tests, in line with our preferred option for the Age Pension (Section 4.4.1).
- It better aligns private contributions with capacity to pay by reducing private contributions for households with limited means, and increasing private contributions for households with substantial means.

Table 8 compares our preferred option and the current means test.

TABLE 8

### Aged Care means test: current vs preferred option

FEATURE	CURRENT MEANS TEST	PREFERRED OPTION
<b>TREATMENT OF OWNER-OCCUPIED HOUSING IN ASSETS TESTS</b>		
<b>Home equity in assets test</b>	Net home equity is capped at a limit of <b>\$214,884</b> for the means test	The first <b>\$500,000</b> of net home equity is excluded. Equity above this amount is included in full
<b>Home exemption</b>	The home is exempt from Aged Care means testing if the recipient or a protected person continues to live there	Exemptions removed
<b>PRIVATE CONTRIBUTION RATES</b>		
<b>Residential – Clinical</b>	Recipients make no contribution to clinical care, regardless of means	Higher means residents can now pay up to the full clinical cost (up to <b>\$250 per day</b> on average)
<b>Residential – Non-clinical</b>	Residents can currently contribute up to about <b>\$200 per day</b> toward non-clinical care costs	Unchanged
<b>Support at Home – Clinical</b>	Recipients make <b>no contribution</b> to clinical care, regardless of means	Higher means recipients can now pay up to <b>80%</b> of clinical costs
<b>Support at Home – Non-clinical</b>	Higher means recipients can now pay up to <b>80%</b> of non-clinical costs	Unchanged

Note: Further detail is provided in Appendix B. Our modelling does not include any change to Aged Care income tests. Private contributions for Residential Aged Care are average benchmarks for modelling purposes, but contributions will vary by location, provider, room type, and care needs.

Source: Policy Institute Australia analysis.

#### 4.5.2 How would this change affect outcomes across the distribution?

Under our preferred option, Aged Care subsidies for those in the bottom 40% of the wealth distribution would increase, due principally to higher government contributions for Support at Home services for full pensioners.

Aged Care subsidies to those in the top 40% of the wealth distribution, and particularly those in the top 20%, would decrease.

Under the current system, the average Aged Care support recipient in the bottom 20% of the wealth distribution receives about 1.5 times as much as the average recipient in the top 20%. Under our preferred option, this ratio increases to 4.5 times, indicating a significantly more targeted distribution of benefits.

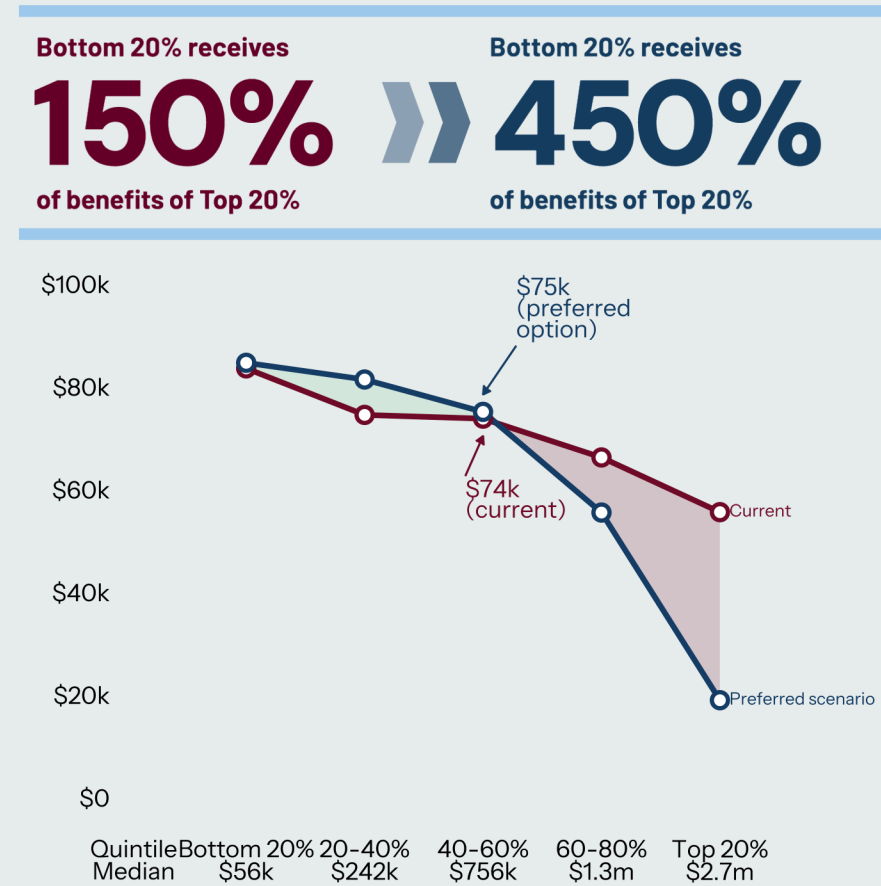
In total, our preferred option would reduce Commonwealth expenditure on Aged Care by around \$6.3 billion a year, with about \$5.2 billion in reduced expenditure for the top 20% of the wealth distribution. These are households with more than \$1.8 million in net assets.

The fiscal savings are significant, though less than for the Age Pension. This reflects the size of the program, and the design of our preferred option, which reflects the particulars of Aged Care. It is partly needs-driven, where people receive care because they have functional, health or daily-living needs. Nonetheless, a better targeted means test should ask those with substantial housing and financial wealth to make a larger contribution to costs that better aligns with their capacity to pay.

FIGURE 18

#### Reform better targets Aged Care support at those with greater need

Average annual Aged Care benefit per current recipient, by wealth quintile



Source: Policy Institute Australia Microsimulation Model (PIAMM).

Currently, around 200,000 people are in Residential Aged Care, and about 380,000 receive Support at Home.<sup>107</sup> Under our proposed changes, around two thirds of these Aged Care recipients would either receive a higher government contribution or see no change – including most of those in the bottom 60% of the wealth distribution, with household wealth of less than \$978,000.

Around a third of Aged Care recipients would receive reduced government contributions. Most of these are in the top 20% of the wealth distribution (Figure 19). A relatively small number of lower wealth recipients of Support at Home also see a reduction in benefits, where their household income makes them ineligible for a full pension (for example, their partner may still work full time); they pay a higher private contribution under our preferred option (Table 8).

The change in contribution varies across recipients. The most significant reductions are for those with substantial wealth, especially those with substantial net equity in owner-occupied housing.

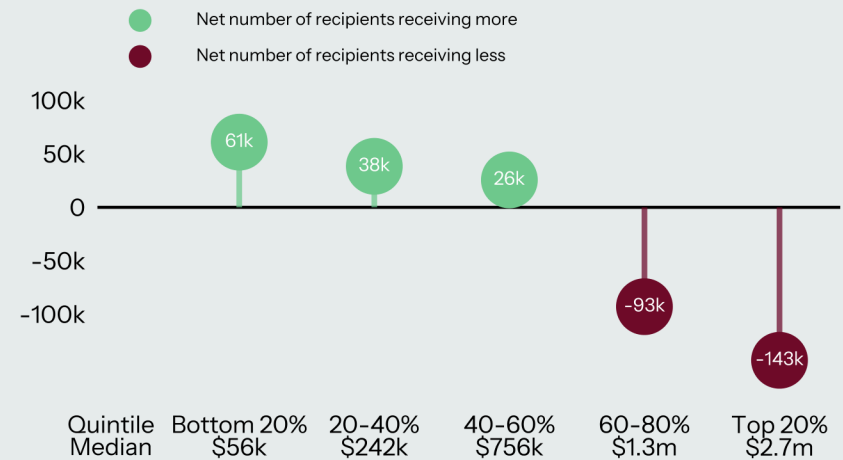
For Aged Care recipients in the top 20% of the wealth distribution, average annual Aged Care support would fall from around \$55,000 per year to around \$19,000. For those in the 60–80% quintile, it would fall from around \$66,000 per year on average to around \$56,000. While for those in the bottom 60% of the wealth distribution, it would increase from around \$77,000 per year on average to around \$80,000 per year.

<sup>107</sup> Australian Institute of Health and Welfare (2025b).

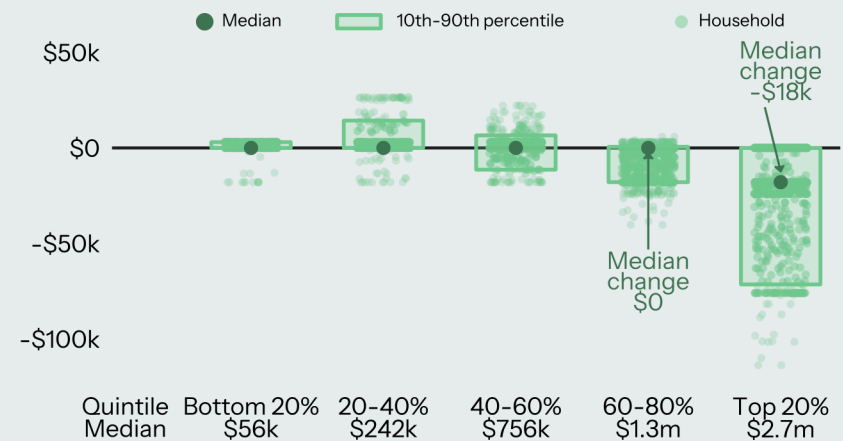
FIGURE 19

**Effects vary across the wealth distribution**

*Net number of current Aged Care recipients receiving more/less, by wealth quintile*



*Distribution of Aged Care payment changes among current recipients, by wealth quintile*



Source: Policy Institute Australia Microsimulation Model (PIAMM).

### 4.5.3 Alternative options

Our preferred option aims to strike a balance between addressing the horizontal and vertical inequities identified above (Section 3.3), while taking account of the particular characteristics of owner-occupied housing and the role of owner-occupied housing for older Australians.

We have modelled two alternative options. Our alternative options match our preferred option, except for how equity in owner-occupied housing is counted in the means tests. Results for all three are presented in Table 9.

The **Full Home Equity** option has the same increase to assets test thresholds for homeowners, but includes the full equity value of owner-occupied housing in the asset test. This option fully addresses the horizontal inequity between homeowners and non-homeowners, and the vertical inequity that follows from treatment of households with different value homes.

The **Home Equity > \$1 million** option has the same increase to assets test thresholds for homeowners, but only the net value of owner-occupied housing above \$1,000,000<sup>108</sup> is included in the assets test. While this option represents a smaller change than our preferred option, it still has the effect of more than doubling the ratio of benefits going to bottom 20% of the wealth distribution, relative to the top 20% (from 1.4 to 3.4).

As noted in relation to the Age Pension, one option would be to set a higher threshold such as \$1 million but to fix it in nominal terms so a greater proportion of owner-occupied housing value is counted over time as house prices rise.

<sup>108</sup> Broadly equivalent to the Australia-wide median home price of \$930,000.

TABLE 9

### Aged Care means test: alternative options compared

FEATURE	FULL HOME EQUITY	PREFERRED: EQUITY >\$500K	EQUITY >\$1M
<b>2025–26 savings</b>	\$8.8 billion	<b>\$6.3 billion</b>	\$3.1 billion
<b>Recipients receiving the same or more support</b>	64.8%	<b>67.0%</b>	77.2%
<b>Share of savings from top 20% by wealth</b>	65%	<b>87%</b>	130%
<b>Ratio: bottom 20% to top 20% avg. support</b>	4.8 (curr. 1.4)	<b>4.5</b> (curr. 1.5)	3.4 (curr. 1.4)
<b>Number receiving less</b>	298,000 people	<b>279,000 people</b>	193,000 people
<b>Home equity where residential support may reduce (couple)</b>	Above ~\$120k	Above <b>~\$620k</b>	Above ~\$1.12m
<b>Home equity where 'Support at Home' may reduce (couple)</b>	Above ~\$730k	Above <b>~\$1.23m</b>	Above ~\$1.73m

Note: Percentages for people receiving less are shares of modelled Aged Care recipients, estimated using calibrated care-type rates. Savings shares can exceed 100% where lower-wealth groups receive net increases, reducing aggregate net savings.

Source: Policy Institute Australia Microsimulation Model (PIAMM).

## 5 Retirement Contribution Scheme

### 5.1 Using wealth to support retirement living standards

The previous section outlined preferred options for better targeted Age Pension and Aged Care supports that account for owner-occupied housing wealth more fairly.

Under our proposed approach, the large majority of retirees impacted by the change would still qualify for a full or part pension upon their retirement. Three-quarters of households receiving the Age Pension would see no change or an increase in the pension they receive.

There are some retiree households who live in relatively high value homes, but do not have other assets with which to support their standard of living. Under our preferred option, these retirees may not qualify for a full pension, and therefore may need assistance to support a standard of living at the full pension rate.<sup>109</sup>

Specifically, we estimate that about 5% of current retiree households<sup>110</sup> would need assistance to maintain the full pension standard of living (Figure 20). A further 14% of older households *may* need assistance at some point in their retirement because the value of the assets they hold would rise over time, eventually equal to the above threshold test – because their home appreciates in value, or they sell non-home assets to meet living expenses, or both.

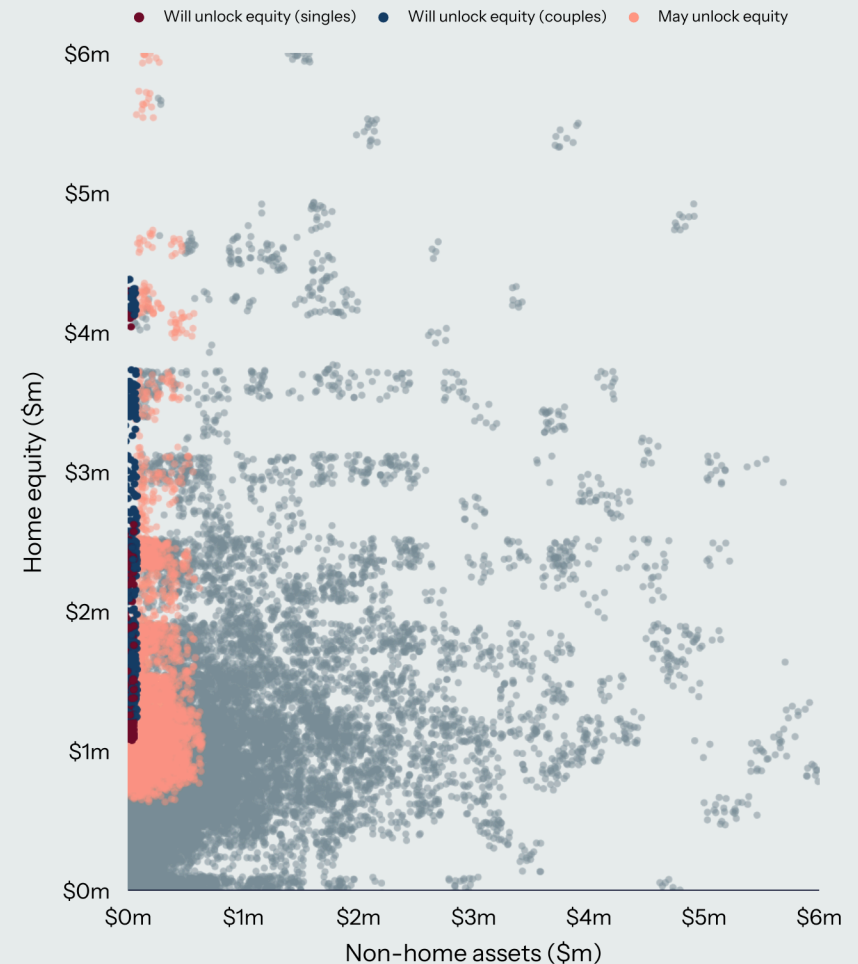
<sup>109</sup> Currently about \$31,200 a year for singles, and \$47,100 a year for couples.

<sup>110</sup> This is about 106,000 households, who would lose full pension eligibility and have less than \$50,000 in non-home assets. Note that this is lower than the 450,000 households that would receive reduced benefits from our proposed changes.

FIGURE 20

### Only a fraction of retirees will need assistance to unlock equity

67+ population; each dot represents around 100 weighted people



Note: We define this group as: for singles, having net owner-occupied housing wealth greater than \$1.08 million, and non-home assets of less than \$50,000; for couples, having net owner-occupied housing wealth greater than \$1.24 million, and non-home assets of less than \$75,000. Jitter applied to show overlapping observations.

Source: Policy Institute Australia estimate using the HILDA dataset (Melbourne Institute, 2025).

## 5.2 Retirement Contribution Scheme (ReCS)

To address the needs of these households, and support the wellbeing of other retiree households, Policy Institute Australia suggests the 'Retirement Contribution Scheme', ReCS, based on the Higher Education Contribution Scheme (HECS), which allows eligible students to defer university tuition fees.

This new idea would allow retired Australians to defer the cost of self-funding their retirement. In this way, older Australians would be able to retain their existing assets, including their home, as well as a full or part pension if they are eligible.

ReCS adopts several design features of the existing HECS:

1. It is a concessional loan, with the value of the loan indexed to inflation.<sup>111</sup>
2. It is income-contingent, and repayment is deferred until the recipient has the capacity to do so. For ReCS, this would likely occur when assets are sold. There would be no forced asset sales, with repayment triggered by the borrower's own decisions or by the eventual transfer of their estate.
3. The scheme is optional, but with administrative arrangements that make it as simple and straightforward as possible to opt-in.
4. The scheme is provided by the Commonwealth Government.

ReCS would have broad eligibility. It would be open to any Australian above the Age Pension age of 67, with sufficient assets against which to secure the loan — such as owner-occupied housing, superannuation or other financial assets.

<sup>111</sup> Note that HECS is indexed to the lower annual growth rate of the Wage Price Index or Consumer Price Index. ReCS would be indexed to the Consumer Price Index.

The loan would be secured against assets, instead of future income earnings as is the case with HECS.

Recipients would be able to access any amount up to 150% of the full pension rate for singles or couples, minus any pension amount currently received. The current full rates (annualised) are equal to about \$31,200 for singles and \$47,100 combined for couples in 2025–26.

Recipients would also be able to use ReCS to fund *any* out-of-pocket Aged Care fees, including accommodation costs (either daily or lump sum), clinical care, hotelling contributions, non-clinical care contributions, daily fees, or higher everyday living fees. For some retirees, this could lead to significantly larger annual borrowings than if ReCS was used only to fund up to 150% of the pension.

Its principal target would be the two cohorts identified above, but for others, ReCS offers the opportunity for some older Australians to increase their standard of living or to defer the cost of self-funding part or all of their retirement. The cap provides certainty over the drawdown rate of the loan and for high wealth households means growth in asset values will likely outpace drawdown rates over the life of the loan.

In addition, any person receiving Aged Care services of any type<sup>112</sup> should be able to access ReCS for any contribution they are required to make for the Aged Care services they receive, as long as they had sufficient assets against which to secure the loan.

The Productivity Commission has previously advocated for a government-backed *Australian Aged Care Home Credit scheme* to be established (as well as for capturing owner-occupied housing in the Residential Aged Care means

<sup>112</sup> Residential Aged Care, Support at Home, or Commonwealth Home Support Programme.

test), which would “help unlock their home equity so they could contribute to their care and accommodation costs while a partner or other ‘protected person’ could continue living in the home.”<sup>113</sup>

Similarly, COTA Australia — the peak body for older Australians — has previously supported a similar idea to enable older Australians to borrow against the equity in their home to pay for aged care services costs. The scheme proposed by COTA would also be HECS-like in its design, in the sense that as people incurred their bills, they would be set against the equity in their home.<sup>114</sup>

ReCS should replace the Commonwealth Government’s existing Home Equity Access Scheme (HEAS). Table 10 outlines the critical ways in which ReCS differs from HEAS, as well as its similarities. The settings of ReCS are such that the private financial sector is unlikely to provide such a product on comparable terms.

The takeup rate of the existing HEAS has been low. There are several elements in the design of ReCS that increase its attractiveness compared to HEAS. Indexation of the loan as per HECS provides more certainty on the total draw down in equity that would result over the life of the loan. This plus the cap on withdrawal to 150% of the pension means the size of the loan is unlikely to grow as rapidly as the value of assets it is held against, meaning that the value of the estate will very likely still be higher than it was at the commencement of retirement. Additionally, the offering of one consistent scheme to support income needs across the pension and aged care systems would simplify an incredibly complex system.

<sup>113</sup> Productivity Commission (2011a).

<sup>114</sup> The Senate Economics References Committee (2015).

TABLE 10

### Comparison of HEAS and ReCS

DESIGN	HOME EQUITY ACCESS SCHEME (HEAS)	RETIREMENT CONTRIBUTION SCHEME (RECS)
<b>Interest rate</b>	Set at ministerial discretion, currently <b>3.95%</b> .	Set as the annual growth in the Consumer Price Index.
<b>Maximum amount to borrow</b>	Up to <b>150%</b> of the applicable pension amount per year, minus any pension received.	Up to <b>150%</b> of the applicable pension amount per year, minus any pension received, plus any Aged Care contributions.
<b>Eligibility</b>	Open to pensioners and self-funded retirees.	Open to pensioners and self-funded retirees.
<b>Security</b>	Australian real estate <sup>*</sup>	Any asset type, including shares, superannuation, investment properties and owner-occupied housing.
<b>Safeguards</b>	No negative equity guarantee	No negative equity guarantee
<b>Payment</b>	Lump sum or regular payment	Lump sum or regular payment
<b>Take-up</b>	<b>19,426 participants</b> in 2026.	Estimated take-up of around <b>126,000 households</b> in 2025–26

Note: Estimated ReCS take-up for 2025–26 comprises 106,000 households with immediate need for assistance unlocking equity plus around 20,000 current HEAS participants. See Section 5.1 for discussion.

<sup>\*</sup> HEAS participants can use real estate assets in Australia as security where the owner holds freehold or equivalent title to the land, and holds adequate insurance. This includes owner-occupied housing, investment properties, and vacant land.

Source: Policy Institute Australia analysis. Department of Social Services (2026a).

This may reduce the tendency for precautionary savings now observed among early-retiree households.

It could also greatly reduce the uncertainty and stress many families experience when making financial arrangements for aged care, where arrangements often need to be made at relatively short notice. The support for these families would be immediate and at a level equal to those received by retirees on lower incomes, but ultimately repaid and therefore at lower cost to taxpayers.

There are some implementation considerations that would need to be worked through for ReCS. However, this paper aims to outline a broad direction for reform and does not intend to solve all implementation issues, although this could be an area for further Policy Institute Australia research.

### 5.3 How would older Australians' living standards and wealth be affected?

This section details how retired Australians in different circumstances would be affected by the 'preferred options' for reforming the Age Pension and Aged Care, along with the proposed introduction of ReCS.

#### 5.3.1 Cameo 1: Josephine owns a median value home, and will continue to receive the Age Pension into retirement

Josephine is a single pensioner who owns a median value Australian home worth \$930,000.<sup>115</sup> She has no other significant assets.

Josephine is currently receiving the full Age Pension, as her other assets fall below the current \$321,000 assets test threshold for single homeowners.

Our preferred option increases the applicable full pension assets test threshold to \$579,000, and excludes the first \$500,000 of owner-occupied housing from the assets test, meaning that Josephine will remain eligible for the full pension, as her assessable assets would be \$430,000.

Over time, the value of Josephine's asset will grow. After a number of years, she will lose eligibility for the full pension and will instead be eligible for a part pension.

ReCS allows Josephine to maintain her standard of living at the same level by borrowing the difference between the full pension rate and the part pension she receives, at zero real interest, secured against her owner-occupied housing.

<sup>115</sup> Cotality (2026).

FIGURE 21

#### Josephine can top up her income with ReCS when she goes to the part pension

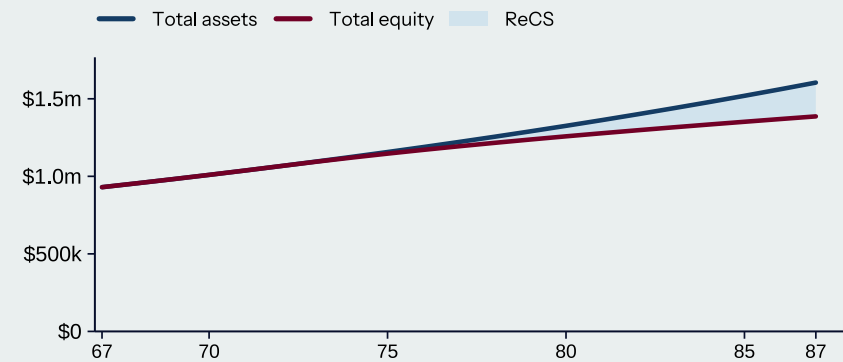
Josephine's balance sheet and assessable assets and debt, real \$2025–26, by age

Age	Composition	House	Other	ReCS	Equity	Pension
67		\$930k	\$0	\$0	\$930k	Full
70		\$1.01m	\$0	\$0	\$1.01m	Full
75		\$1.16m	\$0	-\$10k	\$1.15m	Part
80		\$1.33m	\$0	-\$68k	\$1.26m	Part
85		\$1.52m	\$0	-\$167k	\$1.35m	None
87		\$1.60m	\$0	-\$218k	\$1.39m	None

FIGURE 22

#### Josephine will be \$400,000 richer in 20 years despite losing full pension eligibility during her retirement

Josephine's balance sheet, real \$2025–26, by age



Note: Figures are projected over a 20-year horizon from age 67 in real \$2025–26. This assumes 2.5% annual consumer price inflation, 2.8% real annual home price growth (reflecting the 50-year average in Australia) and an assumed 4.0% real annual return on non-housing assets, including reinvesting any income from assets. Age Pension entitlements are modelled in line with the preferred option in Section 4, with the asset test thresholds assumed to stay constant in real terms.

Source: Policy Institute Australia analysis.

### 5.3.2 Cameo 2: David owns a modest home in regional Victoria, and will receive the full Age Pension for his whole retirement

David is a single pensioner who owns a modest \$400,000 home. He holds no other significant assets.

David is currently receiving the full pension, as his other assets fall below the current \$321,000 assets test threshold for single homeowners.

Our preferred option increases the applicable full pension assets test threshold to \$579,000, and excludes the first \$500,000 of owner-occupied housing from the assets test, meaning that David will remain eligible for the full pension, as his assessable assets would be \$0.

While David continues to receive the same benefits, he chooses to use ReCS to supplement his income. He is eligible to receive an additional 50% on top of the value of his full pension, and chooses to access the full amount, giving him an additional \$600.45 a fortnight in 2025–26, equivalent to \$15,611.70 over the year.

FIGURE 23

### David can boost his cash income while staying on the full pension

David's balance sheet and assessable assets and debt, real \$2025–26, by age

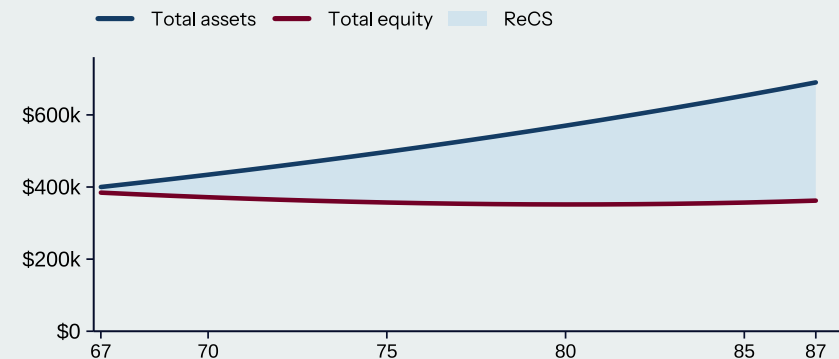
Age	Composition	House	Other	ReCS	Equity	Pension
67		\$400k	\$0	-\$16k	\$384k	Full
70		\$434k	\$0	-\$62k	\$372k	Full
75		\$498k	\$0	-\$141k	\$357k	Full
80		\$570k	\$0	-\$219k	\$352k	Full
85		\$653k	\$0	-\$297k	\$357k	Full
87		\$690k	\$0	-\$328k	\$362k	Full

ReCS House (exempt) House (assessed) Other assets

FIGURE 24

### David's equity draws down slowly while using ReCS to give his income a 50% boost

David's balance sheet, real \$2025–26, by age



Note: Figures are projected over a 20-year horizon from age 67 in real \$2025–26. This assumes 2.5% annual consumer price inflation, 2.8% real annual home price growth (reflecting the 50-year average in Australia) and an assumed 4.0% real annual return on non-housing assets, including reinvesting any income from assets. Age Pension entitlements are modelled in line with the preferred option in Section 4, with the asset test thresholds assumed to stay constant in real terms.

Source: Policy Institute Australia analysis.

### 5.3.3 Cameo 3: Judy, who owns a \$3 million Sydney home, will no longer receive the pension, but can self-fund retirement and will still be richer in 20 years than she is today

Judy is a 67-year-old single pensioner who has \$3 million in owner-occupied housing, as well as \$200,000 in shares.

Judy is currently receiving the full Age Pension, as her assets fall below the current \$321,000 assets test threshold for single homeowners.

Our preferred option increases the applicable full pension assets test threshold to \$579,000, and excludes the first \$500,000 of owner-occupied housing from the assets test, meaning that Judy will no longer be eligible for any pension.

However, Judy can continue to maintain her standard of living — receiving an income stream from ReCS equivalent to the value of her previous pension.

At age 86, Judy needs to go into Aged Care. She can then use ReCS to help fund her Aged Care contributions.

After 20 years, Judy would still be richer than she is today. Assuming 2.8% real annual home price growth (reflecting the 50-year average in Australia), she would see an increase in the real value of her *net* worth of about \$1.5 million<sup>116</sup> — even with an entirely self-funded retirement.

<sup>116</sup> Assuming the 50-year trend residential property price growth and an assumed 4.0% real annual return on non-housing assets, including reinvesting any income from assets.

FIGURE 25

#### Judy maintains her standard of living using ReCS

Judy's balance sheet and assessable assets and debt, real \$2025–26, by age

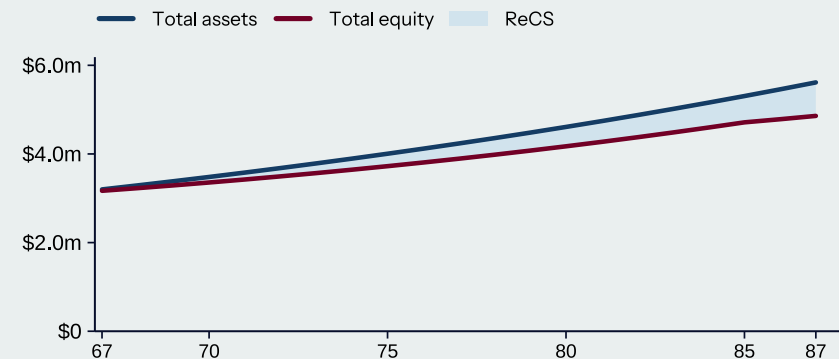
Age	Composition	House	Other	ReCS	Equity	Pension
67		\$3.00m	\$200k	-\$31k	\$3.17m	None
70		\$3.26m	\$225k	-\$125k	\$3.36m	None
75		\$3.73m	\$274k	-\$281k	\$3.72m	None
80		\$4.28m	\$333k	-\$437k	\$4.17m	None
85		\$4.90m	\$405k	-\$593k	\$4.71m	None
87		\$5.18m	\$438k	-\$756k	\$4.86m	None

ReCS House (exempt) House (assessed) Other assets

FIGURE 26

#### Judy's wealth is projected to rise by over \$1.5 million, due to the growing value of her significant assets

Judy's balance sheet, real \$2025–26, by age



Note: Figures are projected over a 20-year horizon from age 67 in real \$2025–26. This assumes 2.5% annual consumer price inflation, 2.8% real annual home price growth (reflecting the 50-year average in Australia) and an assumed 4.0% real annual return on non-housing assets, including reinvesting any income from assets. Age Pension entitlements are modelled in line with the preferred option in Section 4, with the asset test thresholds assumed to stay constant in real terms.

Source: Policy Institute Australia analysis.

## 5.4 What would be the cost to taxpayers?

As discussed in Section 5.2, ReCS would allow some retirees to defer their living expenses, by borrowing from the Commonwealth Government at a zero real interest rate. The loan is paid back, but only when assets are sold.

From the perspective of the Commonwealth Government, ReCS will in many cases represent a switch from annual budget expenditure to a loan provided to participants at a concessional rate. It will show up in the Commonwealth budget in three ways.

First, when an Australian of pension age decides to opt in to the scheme, the Commonwealth Government lends them *up to* 150% of the applicable full pension rate (less any pension they may currently receive, and plus any Aged Care contributions). This will appear on the Commonwealth's balance sheet as a loan, which is a *financial asset*.<sup>117</sup>

Second, the Commonwealth Government incurs the operational cost of carrying the loan. Borrowers pay zero real interest (the loan is indexed to inflation), while the Commonwealth Government will borrow at a higher nominal rate. Assuming average inflation of 2.5%,<sup>118</sup> and a Commonwealth Government borrowing cost of 5%,<sup>119</sup> the cost to the taxpayers of carrying the loan would be 2.5% of the loan value each year. This represents the major fiscal cost to the scheme.

Third, when retiree households' assets are sold or transferred, the loan principal

<sup>117</sup> There are many government loans currently like this on the Commonwealth's balance sheet. The existing HECS program is the largest, at over \$40 billion (Department of the Treasury, 2026a).

<sup>118</sup> The midpoint of the RBA's target band.

<sup>119</sup> Representing the current 10-year Commonwealth Treasury rate (Trading Economics, 2026).

(plus indexation) is repaid in full to the Commonwealth Government. There are no forced sales, with repayment triggered by the borrower's own decisions or by the eventual transfer of their estate. As the Commonwealth notes, all loans given out contain some element of credit risk that they will not be repaid in full,<sup>120</sup> but for ReCS, this would be very low given that loans are secured against assets and the borrowing amounts are comparatively low.<sup>121</sup>

Forecasting the total future cost to taxpayers of ReCS would be a significant undertaking, and heavily dependent on assumptions, and is beyond the scope of this report.

Instead we present cameos (aligning with those presented above) to show the cost to taxpayers for several different household types and decisions, relative to the savings from reduced expenditure on Age Pension and Aged Care to these households (Figure 27).

To summarise, where ReCS is used to fund a reduced government benefit (as with Cameos 1 and 3), taxpayers can expect substantial overall savings. Where ReCS is used without any reduced benefit (as with Cameo 2), taxpayers can expect a more modest (although still significant) additional cost.

### 5.4.1 Estimated takeup

In Section 5.1, we estimated that our proposed changes to the pension assets test would result in about 5% of current Australian retiree households requiring ReCS to meet living expenses equivalent to the full pension rate, and that an additional about 14% of this current cohort *may* need to use ReCS at some point

<sup>120</sup> Department of the Treasury (2026a).

<sup>121</sup> The Department of Social Services advised that, for HEAS, the risk of non-recovery for loans is very low, due to requiring security against land and the Commonwealth's debt recovery powers.

during their retirement. All of these households would see reduced pension benefits.

This is a large group, and implies that ReCS loans could become a large asset on the Commonwealth Government’s balance sheet. However, the overall savings to taxpayers would far outweigh the cost over time.

We expect that take-up of ReCS would be limited outside of this group, based on the fact that current take-up of the Home Equity Access Scheme (HEAS) is very low. As at March 2026, there were 19,426 participants using HEAS, representing less than 0.5% of the retiree population.<sup>122</sup> While ReCS is likely to be more attractive to some retirees (Table 10), we expect that takeup would follow a similar pattern among retirees who have no need to borrow in order to support their living expenses while remaining in their home. Consequently, the cost to taxpayers of providing ReCS to this group is likely to represent only a small fraction of the overall savings. If take-up among this group was much higher than expected, especially among wealthy or high-income retirees, then safeguards could be introduced.

FIGURE 27

**ReCS is likely to cost a fraction of expected savings**

*Estimated fiscal impact of ReCS across the three cameos, over twenty years, real \$2025–26*



Note: Figures rounded to the nearest \$1,000 (totals) and \$100 (annual averages). Operational servicing cost is the average annual cost to government of carrying the ReCS debt over the life of the debt. This is an estimated 2.5% per year.

Source: Policy Institute Australia estimates.

<sup>122</sup> Department of Social Services (2026a); Australian Bureau of Statistics (2025a).

## 6 Conclusion

Australia's social safety net has long reflected a simple idea: taxpayer-funded support should go to those who need it most. That idea has quietly lost ground. Over recent years, a growing share of support has gone to households with the greatest capacity to support themselves — including households in the top 20% of Australia's income or wealth distribution.

The rules we use to determine who needs support from taxpayers have not kept pace with an ageing, wealthier population. The result is a system that significantly underestimates the true financial capacity of many Australian households, while heavily favouring those who hold their wealth in owner-occupied housing over those who hold it in other forms.

This report has proposed an evolution in Australia's approach to means testing, informed by the principles of equity and sustainability. We have developed and modelled alternative income and assets tests for four major programs — the Child Care Subsidy, Parental Leave Pay, the Age Pension, and Aged Care — and suggested a new policy, ReCS, to ensure that retirees affected by fairer means testing can maintain their standard of living.

Our preferred options would reduce outlays across these four programs by around \$21 billion in 2025–26. Most of this saving comes from the top 20% of households by wealth or income — households with the capacity to pay for more of their needs themselves. Our reforms would shift the distribution of benefits across all four programs closer to what some of Australia's well-targeted cash transfer programs already achieve, directing more support to those with the greatest need.

The scale of potential savings is significant. Freeing \$21 billion in funding could, for example, cut the tax rate for all income tax thresholds by 1.7 percentage points, which would reduce personal income taxes by up to \$2,000 for Australians in the middle income bracket and up to \$8,000 for those in the top bracket; or provide \$5,000 more per year in benefits to the 4.4 million or so households in the bottom 40% of the income or wealth distribution; or pay down around 70% of the current year fiscal deficit for the Commonwealth. Even a fraction of these savings could fund meaningful increases in supports targeting those most in need — in 2025–26, total expenditure on JobSeeker was \$16 billion and on Rent Assistance it was \$7 billion.

The intention of this analysis is not to provide a definitive answer on how means testing should be designed for these programs. Rather, it aims to illustrate the magnitude of the loss in equity and sustainability that is building from our current approach, and to suggest a direction for reform. Nor is our list of four programs intended to be exhaustive. There are other social transfers that are poorly targeted, and many large in-kind programs that are not means tested at all. The programs modelled here demonstrate what a more equitable and sustainable approach could look like, not where reform should start or stop.

This report aims to kick-start a conversation Australia needs to have. Our social compact depends on it.

## A Child Care Subsidy – disincentives to work

Workforce disincentive rates are important tools to assess the effect that policy changes can have on workforce participation. The charts below outline the workforce disincentive rates under a set of cameos that show the current settings and our preferred options (outlined in Section 4).<sup>123</sup> A disincentive rate of, for example, 40% means that for every dollar earned, the parent takes home 60 cents in pay.

This analysis builds on that presented in Section 4.2.3 in relation to households with parents able to earn the median full time employed wage of \$100,000 a year. Incomes are varied in the cameos below, but other assumptions outlined in that section apply here, including that: in dual parent families, one parent is assumed to work full time; and children below school age are assumed to be in paid child care for the same number of days as the single or second parent works.

### Disincentives to work are reduced for many lower-income households under the preferred option

Disincentives to work for lower-income households are reduced under our preferred option for two reasons. First, the Child Care Subsidy rate has been *lifted* to 95% (from 90%) for lower-income families, reducing net child care

<sup>123</sup> This captures the interaction of the existing tax and transfer system (such as, for example, income taxes, and other social transfers such as Family Tax Benefit A and B), as well as the 'net child care' effect (which captures the out-of-pocket costs for parents to send a child to an additional day of child care and any phase out in the Child Care Subsidy received).

costs. Second, the taper begins later in the income distribution – with the maximum subsidy (95%) available for all families up to \$133,000 of pre-tax income (compared to \$85,279 now).

For a single parent earning \$71,000,<sup>124</sup> workforce disincentive rates are improved (i.e. reduced) across each day of additional work (Figure 28). For that same parent, with a partner also earning \$71,000, workforce disincentive rates are improved for the first four days of work.

### Disincentives to work are reduced for some families with two children under the preferred option

Under our preferred option, families with two children in child care have generally better workforce disincentive rates if they have a combined pre-tax household income of up to \$250,000. This is because of the design to the taper rate for the second child in paid care. The two children cameos for the lower-income household in Figure 28 and for the single parent in Figure 29 illustrate this point – with lower workforce disincentive rates for the second child in child care.

### Disincentives to work are worse for some higher-income families

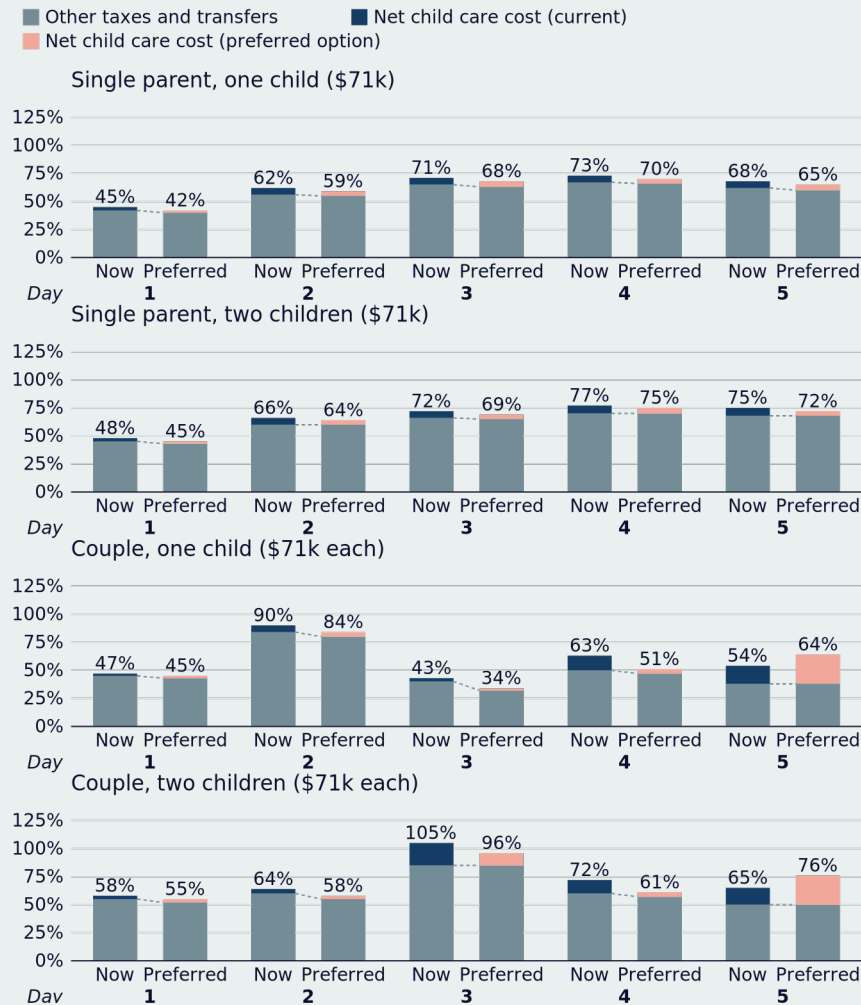
One of the trade-offs of our preferred option is that disincentives to work are worse for some higher-income families. This is an inevitable feature of having more targeted means testing, as, by design, higher-income families face higher out-of-pocket costs for placing children in paid child care. A \$71,000 earner faces generally higher disincentives to work if they have a high-income partner, with much higher disincentives for the fourth and fifth day (Figure 30).

<sup>124</sup> the 20th percentile of earnings of full-time employees.

FIGURE 28

**Workforce disincentive rates tend to be reduced for lower-income households, where parents can earn \$71,000 a year**

Workforce disincentive rate shown includes average child care cost net subsidy, plus taxes and the phase out of other transfers



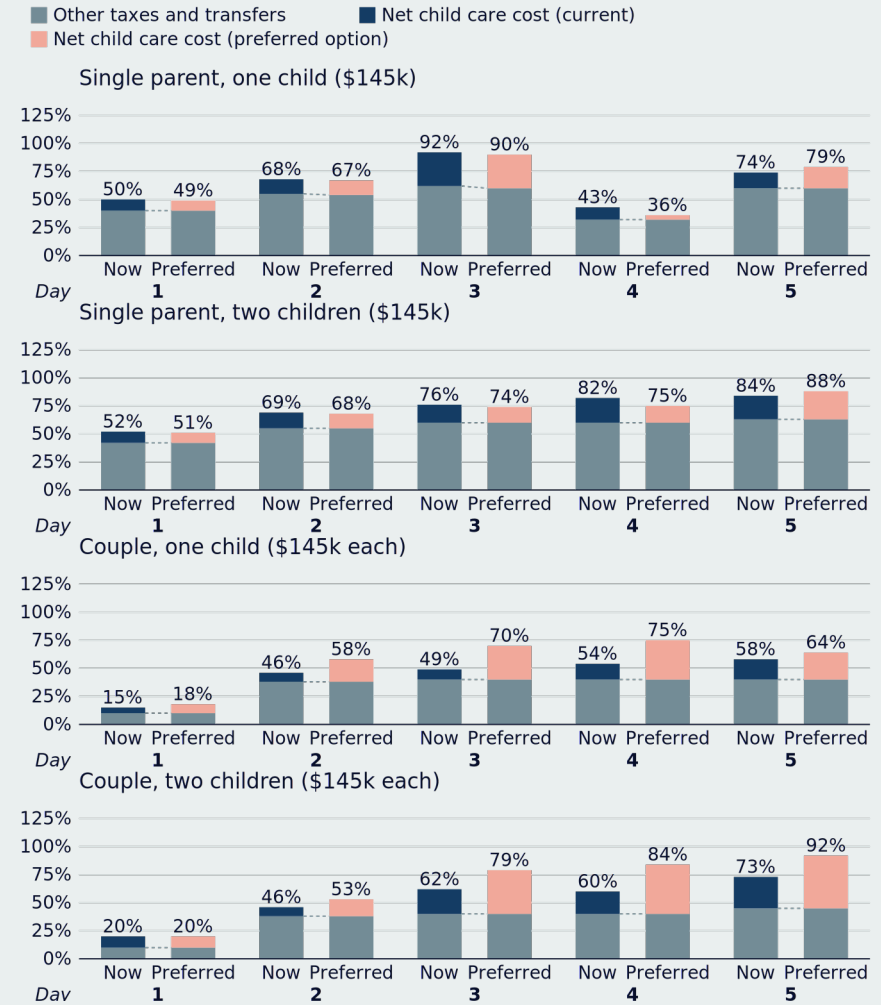
Note: This figure shows the workforce disincentive rates for a parent who earns \$71,000 per year when working full time. The cameos vary whether they are single or have a partner (also earning \$71,000 per year) and the number of children in child care (one or two).

Source: Policy Institute Australia modelling.

FIGURE 29

**Workforce disincentive rates may be higher or lower for higher-income households, where parents earn \$145,000 a year**

Workforce disincentive rate shown includes average child care cost net subsidy, plus taxes and the phase out of other transfers



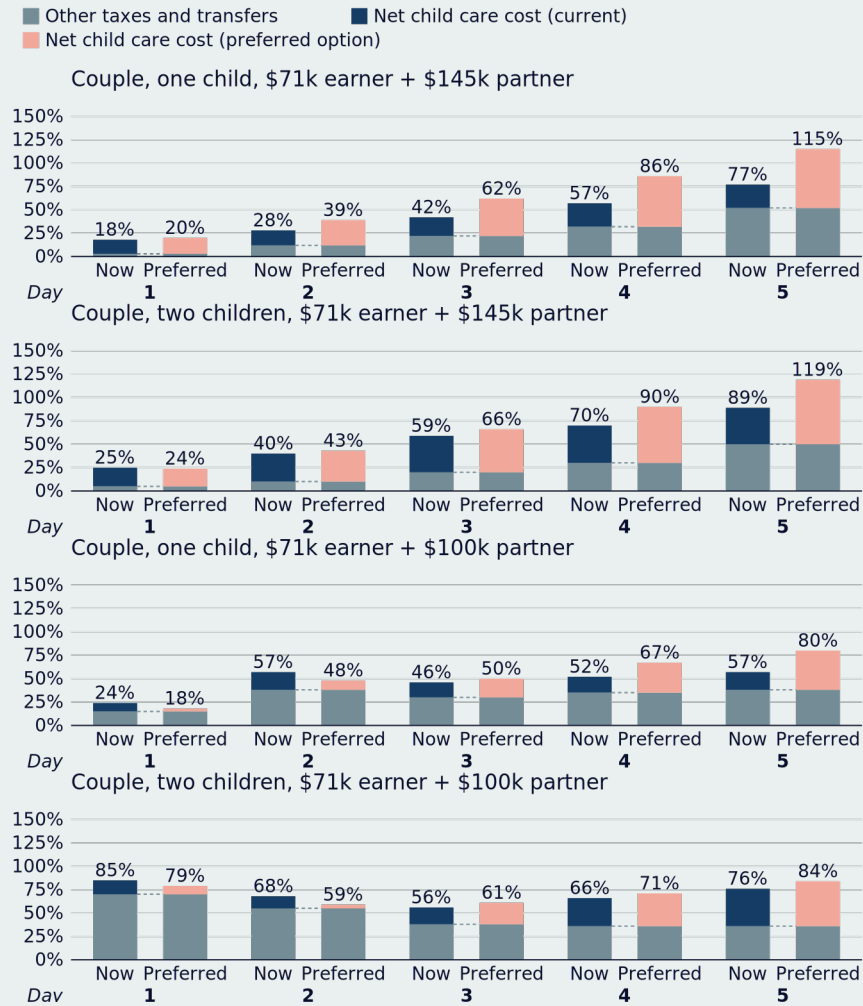
Note: This figure shows the workforce disincentive rates for a parent who earns \$145,000 (the 80th percentile of earnings of full-time employees) per year when working full time. The cameos vary whether they are single or have a partner (also earning \$145,000 per year) and the number of children in child care.

Source: Policy Institute Australia modelling.

FIGURE 30

### Workforce disincentive rates are generally higher for couples with disparate earning capacity

Workforce disincentive rate shown includes average child care cost net subsidy, plus taxes and the phase out of other transfers



Note: This figure shows the workforce disincentive rates for a parent who earns \$71,000 per year when working full time. The cameos vary whether their partner earns \$145,000 or \$100,000 and the number of children in child care (one or two).

Source: Policy Institute Australia modelling.

## B Aged Care means testing arrangements

TABLE 11

### Residential Aged Care fees and contributions: current settings vs. preferred option

COST / SERVICE CATEGORY	WHAT IT COVERS	CURRENT SETTINGS	PREFERRED OPTION
<b>Clinical care</b>	Nursing, medication management and other clinical care.	<b>\$0.</b> Government fully funds clinical care.	Residents can pay up to 100% of their clinical care (up to about <b>\$250 per day</b> on average) depending on means. This is only paid if means are sufficiently high that the resident pays <b>100%</b> of the hotelling contribution, non-clinical care contribution and accommodation contribution.
<b>Hotelling contribution</b>	Additional contribution to daily living and hotel-type services.	Up to <b>\$22.15 per day</b> , depending on means; no annual or lifetime cap.	Unchanged.
<b>Non-clinical care contribution</b>	Personal and non-clinical care, such as bathing, mobility assistance and lifestyle activities.	Up to <b>\$107.32 per day</b> , depending on means; capped at <b>\$137,917.01</b> lifetime, or four cumulative years, whichever comes first.	Unchanged.
<b>Accommodation costs</b>	The room or accommodation place.	Low-means residents may receive government assistance; others pay the agreed room price as a lump sum, daily amount or combination.	Unchanged.
<b>Basic daily fee</b>	Standard daily living costs, such as meals, cleaning, laundry and utilities.	<b>\$66.80 per day</b> ; generally paid by everyone, regardless of means.	Unchanged.
<b>Higher everyday living fee</b>	Optional extras or higher-standard services agreed with the provider.	Optional; agreed with provider; not part of the means-tested Aged Care contribution cap.	Unchanged.

Note: Means testing is based on income and assets. Under the preferred option, residents with sufficiently high means may pay the full hotelling contribution, non-clinical care contribution and accommodation contribution.

Low-means residents receive greater government support. For couples, half of combined income and assets is counted. The family home can be counted up to a capped value unless a protected person lives there.

Source: Policy Institute Australia analysis.

TABLE 12

**Support at Home recipient contributions: current settings vs. preferred option**

CARE TYPE	WHAT IT COVERS	CURRENT SETTINGS	PREFERRED OPTION
<b>Clinical care</b>	Care delivered or overseen by health professionals: nursing, allied health. Does not include services provided by a GP or specialist, which are funded through Medicare.	Full pensioner 0%; Part pensioner 0%; Self-funded 0%.	Full pensioner 0%; <b>Part pensioner 0–80%;</b> <b>Self-funded 80%.</b>
<b>Independence</b>	Support to maintain function and independence at home: transport, respite for carers.	Full pensioner 5%; Part pensioner 5–50%; Self-funded 50%.	<b>Full pensioner 0%;</b> <b>Part pensioner 0–80%;</b> <b>Self-funded 80%.</b>
<b>Everyday living</b>	Help with day-to-day tasks: domestic assistance (cleaning, laundry), meals, gardening, home maintenance.	Full pensioner 17.5%; Part pensioner 17.5–80%; Self-funded 80%.	<b>Full pensioner 0%;</b> <b>Part pensioner 0–80%;</b> Self-funded 80%.

Note: Information presented here relates to our preferred option and supplements information outlining the option in Section 4.5.1 and Table 8. 'Part pensioner' includes self-funded retirees with a Commonwealth Seniors Health Card. Our modelling assumes that pension qualification moves in line with our Age Pension preferred option outlined in Section 4.4.1. Part pensioners pay a sliding-scale rate between the full-pensioner and self-funded rates. 'Self-funded' includes people who do not disclose their means.

Source: Policy Institute Australia analysis.

## C Policy Institute Australia

### Microsimulation Model (PIAMM)

#### Overview

Policy Institute Australia has developed a static microsimulation model to estimate the distributional and fiscal effects of alternative means testing arrangements across four major Commonwealth programs: the Age Pension, Aged Care, Child Care Subsidy and Parental Leave Pay.

The model uses detailed household and individual-level survey data from the Household, Income and Labour Dynamics in Australia survey (HILDA). HILDA provides a rich view of household composition, income, labour force status, housing tenure, assets, liabilities, superannuation and family circumstances. This paper uses unit record data from the Household, Income and Labour Dynamics in Australia (HILDA) Survey. The HILDA Project was initiated and is funded by the Australian Government Department of Social Services (DSS) and is managed by the Melbourne Institute of Applied Economic and Social Research (Melbourne Institute). The findings and views reported in this paper, however, are those of the authors and should not be attributed to either DSS or the Melbourne Institute.

#### Modelling units

Policy rules are implemented at the person and income-unit level, reflecting the way Australian tax and transfer settings operate in practice. A *person* is an individual HILDA record, identified using the longitudinal person identifier

and carrying person-level characteristics such as age, sex, labour force status, income, tax liability and individual transfer entitlements.

An *income unit* is the model's family-level assessment unit, constructed from the HILDA household identifier and HILDA income-unit identifier. It generally represents a single adult, or a partnered couple, together with their dependent children, and is used for policy settings that assess resources jointly across a family or couple. Some source variables, particularly wealth, housing and rent variables, are observed at the broader household level and are attached to people and income units for the purposes of means testing.

For readability, references in this report to a "household" or a "family" should generally be read as referring to the modelled income unit, unless the text is explicitly discussing household-level survey variables such as housing, assets or rent.

With the modelling units established, the model then prepares the underlying data for the policy year.

#### Uprating

Before policy rules are applied, the model uprates the HILDA dollar variables to 2025–26. Uprating is applied to the raw income, asset and debt variables before derived concepts such as private income, taxable income, assessable assets, home equity and net worth are constructed. This means the downstream tax and transfer calculations are based on policy-year income and wealth concepts rather than survey-year nominal values.

Uprating is implemented using a set of variable-group growth factors stored in the model's uprating workbook. Separate growth factors are available for

variables sourced from the main survey wave and variables sourced from the wealth wave. Wages and business income are uprated using a Wage Price Index-based factor, CPI-linked income items using CPI, rent variables using the CPI rents series, residential property values using a residential property-price index, superannuation balances using an APRA median balanced fund return proxy, and bank-account balances using a CPI proxy.

After uprating, aggregate balance-sheet variables are recomputed from the uprated components. In particular, household financial assets and total household assets are recalculated, and derived measures such as home equity, business equity and net worth are reconstructed from the uprated asset and debt values.

The uprating process changes dollar values but does not otherwise change household composition, labour-force status, child care hours, eligibility characteristics or population weights. Child care prices are uprated, but reported hours of care are held fixed. The model also does not use uprating to project the population forward by age, sex or state; population alignment is handled separately through the survey weights and subsequent calibration.

The uprating process also exposes a structural feature of HILDA that requires additional treatment: detailed wealth data are not collected in every survey wave.

## Survey design and imputation

HILDA does not collect the full set of wealth variables in every wave. In the model, current demographics, income and labour-force information are taken from wave x (2024), while detailed wealth variables are merged in from wave v

(2022) using the longitudinal person identifier. Housing is treated separately where needed, because some home value and mortgage variables are available in wave x as all-waves housing variables, while broader balance-sheet measures such as financial assets, superannuation and other property wealth come from wave v.

Where a person appears in the main HILDA wave but does not have a matched record in the wealth wave, the model retains the person and flags them as having imputed wealth. Missing non-housing wealth components are imputed using median values from otherwise observed records grouped by age band, homeownership status and couple status.

With the survey data prepared, the model applies a set of policy rules covering the main Commonwealth tax and transfer programs.

## Policy rules

The model includes the main personal income tax and transfer settings, including personal income tax, the Low Income Tax Offset, the Seniors and Pensioners Tax Offset, the Medicare levy, the Medicare levy surcharge, imputation credits, an approximation of superannuation guarantee contributions tax, the Age Pension, Disability Support Pension, JobSeeker Payment, Parenting Payment, Commonwealth Rent Assistance, Family Tax Benefit A, Family Tax Benefit B, the Child Care Subsidy, Parental Leave Pay, residential aged care, Home Care Packages, and Commonwealth Home Support Programme. Each policy draws on income and wealth definitions tailored to its means test.

For several programs, HILDA does not provide a complete or reliable administrative recipient flag, so the model does not simply reproduce reported

receipt. Instead, it simulates entitlement under the relevant policy rules using observed characteristics in the survey. For the Age Pension, the model assesses people against age, income and asset-test rules; for Parental Leave Pay, it identifies potential recipients from the presence of a newborn and assesses them against income and work-test proxies; and for the Child Care Subsidy, it assesses families using observed child care use, child ages, activity-test proxies, hourly fee caps and family income. The model therefore estimates policy entitlement rather than modelling every administrative take-up decision at the individual level. Where available, calibration then benchmarks modelled recipient counts and expenditure against external administrative or budget totals.

HILDA does not report the prices of child care and aged care services directly, so the model estimates these using external benchmark price data. Child care prices are based on Department of Education average hourly fee data, with prices varying by location and type of care; where direct local prices are not available, the model uses state-level averages or closely related fee proxies. Aged Care prices are based on 2025–26 program cost benchmarks: residential care uses an average daily care funding amount plus accommodation and hotelling components, Home Care Packages use annual package budgets, and CHSP uses average unit costs for each service type.

Income uses several policy-specific definitions:

- *Private income* is the base measure, covering wages and salary, business income, investment income, rental income, dividends and private pension income.
- *Adjusted taxable income* applies to family-style tests including Parental

Leave Pay, Family Tax Benefit and the Child Care Subsidy, adding imputation credits, investment add-backs and reportable superannuation contributions.

- *Taxable income* is used for personal income tax, adding imputation credits and taxable transfer payments such as the Age Pension, Disability Support Pension, JobSeeker and Parenting Payment.
- Pension-style means tests replace actual financial investment income with deeming.
- Where a policy assesses income jointly, the model sums the relevant measure across adults in the income unit.

Wealth is also policy-specific:

- The model draws on HILDA household data covering financial assets, superannuation, vehicles, other non-financial assets, housing and debts, uprated to the policy year.
- For pension-style asset tests, the model excludes the principal home, adds household contents as a deemed amount, and excludes superannuation for people below Age Pension age.
- Deeming applies to a financial-assets base with the same age-specific superannuation treatment.
- For aged care, the model may include part of the principal home depending on whether the case is protected or unprotected. For couples, the included equity of the principal home is split between partners before being passed to the asset test.
- For distributional analysis, the model defines wealth more broadly as assessable assets plus home equity, better reflecting households' true

economic resources.

These tailored income and wealth definitions ensure that each program is assessed against the resource concept its legislation specifies. The modelled entitlements are then used as inputs to the calibration process, which aligns the model to external administrative benchmarks.

## Calibration

Calibration is implemented as a constrained reweighting of the HILDA survey weights. After the baseline tax, transfer and aged care calculations are run, the model constructs a calibration matrix in which each column represents an external benchmark target and each row represents a survey person who contributes to at least one target. The cell value is the modelled quantity to be matched: for example, modelled net tax in an ATO tax cell, an Age Pension recipient indicator in a DSS recipient cell, or modelled expected aged care cost for an aged care aggregate.

The calibration solves for a new set of person weights that remain as close as possible to the original HILDA weights while improving fit to the benchmark targets. Formally, the optimisation minimises a Kullback–Leibler divergence term between the calibrated and original weights, plus a large penalty on the squared normalised difference between weighted model totals and external targets. The total weight of the participating sample is preserved exactly, and each calibrated weight is constrained to remain within specified lower and upper bounds relative to its original survey weight. In the current model run, calibrated weights are bounded between 0.05 and 21.0 times the original HILDA person weight, and the target-error penalty is set at  $10^7$ .

Calibration targets are treated as soft calibration targets rather than exact hard constraints, except for the total-weight constraint. This allows the model to balance target fit against preservation of the original survey weight structure. After calibration, the new weights are used for both the current-policy baseline and all reform scenarios, so estimated policy impacts reflect changes in policy settings rather than changes in the underlying population. Records that do not participate in any calibration target retain their original HILDA weight.

## Aged Care modelling

Aged care requires additional modelling because people in residential aged care are not directly observed in HILDA's private-dwelling survey frame. The model therefore estimates aged care exposure for the older population using administrative recipient counts and geographic, age and sex patterns, then calibrates expected costs to published aged care totals.

## Outputs and limitations

The model generates outputs by changing selected policy settings — principally the income and asset test parameters for the Age Pension, Aged Care, the Child Care Subsidy and Parental Leave Pay — and recalculating entitlements for the same underlying population. It then compares each person's or household's entitlement under current policy with their entitlement under the alternative settings. The model aggregates these differences using population weights to estimate changes in total program spending, the number of people or households affected, average gains and losses, and how those changes are distributed across income and wealth groups.

The model is intentionally static. It estimates first-round effects in a single policy year and does not project future population change, macroeconomic feedback, changes in labour supply, asset restructuring, take-up behaviour or long-run care transitions.



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